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January 11, 2001

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BY HAND

The Honorable Vernon A. Williams, Secretary
Surface Transportation Board
Office of the Secretary
Case Control Unit
Attn: STB Ex Parte No. 582 (Sub-No. 1)
1925 K Street, NW
Washington, DC 20423-0001

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Office of the Secretary
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Re: STB Ex Parte No. 582 (Sub-No. 1),
"Major Rail Consolidation Procedures"

Dear Secretary Williams:

Enclosed for filing in the above-referenced matter are an original and 25 copies of the Rebuttal Comments of CSX Corporation and CSX Transportation, Inc., and its Appendix, a Verified Statement of Dr. Robert D. Willig, together with WordPerfect diskettes. A certificate of service follows the text of the Comments, and the Attachment and Appendix follow.

Kindly date-stamp the extra copy of this letter and the Reply Comments, which our messenger is presenting, and return them to the messenger.

If there are any questions concerning this matter, please call the undersigned at (202) 942-5858.

Sincerely yours,

Dennis G. Lyons
Counsel for CSX Corporation and
CSX Transportation, Inc.

rjm
Enclosures
cc All Parties of Record

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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

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January 11, 2001

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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

REBUTTAL COMMENTS OF CSX CORPORATION AND CSX TRANSPORTATION, INC.

Pursuant to the Board's Notice of Proposed Rulemaking ("NPR") served October 3, 2000, and further to their Opening Comments filed on November 17, 2000, and their Reply Comments filed on December 18, 2000, CSX Corporation and CSX Transportation, Inc., submit these Rebuttal Comments on the proposed rules governing major rail consolidations set forth in the NPR.[1]

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[1] We will refer to the Advance Notice of Proposed Rulemaking served March 30, 2000, as "ANPR." CSX Corporation and CSX Transportation, Inc. will collectively be referred to as "CSX." Conventional abbreviations will be used for other carriers and short names or abbreviations for other commenters. The existing railroad consolidation regulations found in Part 1180 of Title 49 C.F.R. will be referred to by the section numbers in Title 49 without repetition of the identification of that Title. The regulations proposed in the NPR will be referred to as "Proposed § 1180.x" as identified in the NPR. "Merger" and "Consolidation" will be used interchangeably to refer not only to statutory mergers and consolidations, but also to other forms of combination of substantially all the properties of two rail carriers into a common control.

INTRODUCTION

This rulemaking procedure has drawn many comments from all quarters involved in the transportation business and there have been many constructive suggestions. In addition, since the last round of comments were prepared, the Board has issued a rate study by its Office of Economics, Environmental Analysis, and Administration, and a decision in the Board's oversight of the UP/SP merger, each of which strongly supports a number of CSX's proposals concerning competition issues and undermines arguments by certain shippers, shortlines and others regarding reregulation and forced "competitive enhancements." CSX will address below the comments and will discuss how the rate study and the oversight decision relate to the issues CSX has already raised.[2]

The rate study and oversight decision both support the proposition that market-driven competition has benefited not only railroads but shippers and their customers, and indeed ultimate consumers as well. The removal of regulatory barriers to rational economic decisionmaking by suppliers of rail service and their customers and the beneficial results of past consolidations have caused railroads to earn a return that permits them to be economically viable (although generally not

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[2] Once again, failure to respond to any of the extensive comments should not be interpreted as assent to them. *See* CSX Reply Comments at 6 n.2.

equal to their cost of capital). At the same time deregulation has driven down the cost of service to shippers and ultimate consumers. This legacy of the Board and its predecessor should be protected, and not undermined by changes in merger review methodology. Thus, as the Board "raises the bar" of competition analysis in its public interest calculus, it should ensure that the very things that have led to a more competitive market — cost savings; economies of scale, scope and density; and other efficiencies — are not thrown out with the bath water of outdated or outmoded procedures that should be changed. Thus, the Board should not adopt a merger review methodology that fails to recognize the positive impact of the efficiencies associated with end-to-end mergers. While CSX and nearly all commenters agree that the Board's long-standing presumption in favor of mergers should be discarded, a large portion of the Board's merger precedent and process remains well suited to the task. Clearly some refocusing needs to be done, and among other things the Board's proposals as to Downstream Effects, Transborder Issues, and Service Assurance are well taken in whole or substantial part.

In contrast, many commenters have called for an all-out reregulation of the industry which would undermine the benefits that the Board's rate study has demonstrated those same parties have received from past deregulation. Other commenters have attempted to bring reregulation in the back door by advocating that the Board use its merger procedures and standards in ways that would produce the same inefficient result. The Board has so far avoided these pitfalls, but the proposed rules still contain provisions that could undermine the benefits gained by the Staggers Act and by well-thought-out mergers. As demonstrated previously and below, and as shown vividly in the appended Verified Statement of Dr. Robert D. Willig, the proposed rules which call for applicants to proffer, and which encourage third parties unaffected by the competitive effects of the merger to seek, unrelated "competitive enhancements," would turn the merger review process into a regulatory morass and consequently discourage "good" end-to-end mergers that otherwise might be proposed. As demonstrated previously and in the present filing, "competitive enhancements" that are unrelated to prospective merger harms will not enhance competition but will only undermine it. They would serve as a form of reregulation that would undercut the benefits that have flowed from efficiencies in the form of economies of scale, scope and density and other cost savings that the Board and its staff have documented. The Board should avoid undermining those efficiencies with what will assuredly be inefficient forms of forced access labeled as "competitive enhancements."

Finally, the Board should encourage a timely and efficient merger review process. Moreover, the Board has already recognized that some cost savings can be realized through joint marketing and other arrangements that do not involve a change in control of Class I railroads. To the extent that any such arrangements are within the Board's jurisdiction, those arrangements should be reviewed swiftly and efficiently in order that their benefits be delivered to the marketplace without undue procedural delay.

I. END-TO-END MERGERS ARE NOT INHERENTLY ANTICOMPETITIVE AND THE BOARD SHOULD NOT PRESUME THEM SO.

The Board's proposed rules presume potential harms from prospective Class I mergers and seek to remedy or balance those harms through a requirement of "enhancements" unrelated to any specific likely harms caused by the merger. Proposed Rule § 1180. Many shippers have advocated that further Class I consolidations are presumptively bad,[3] and various among them have championed reregulation as the best means of addressing these predicted effects. In its earlier filings, CSX demonstrated that the presumption of generalized ill effects requiring a concomitant basket of unrelated "enhancements" is neither necessary nor likely to create public benefit. CSX Opening Comments at 25-29. Since CSX's Opening filing, the Board has released a study involving rail rate decreases[4] and the UP/SP

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3 *See, e.g.*, Joint Reply Comments of "Certain Coal Shippers" at 2, PPL Generation Reply Comments at 6, and Dow Reply Comments at 3.

4 Rail Rates Continue Multi-Year Decline, Office of Economics, Environmental Analysis, and Administration, STB, December 2000 ("The Board's Staff Study").

merger oversight decision that buttress CSX's prior positions.[5] Based on these analyses, the appended Verified Statement of Dr. Robert Willig and the December round of comments, CSX will demonstrate in this section that presuming harmful effects of future mergers is economically unsound, will serve to undermine potential merger benefits and should not be codified in the Board's final rules.

The Board's Proposed Rule § 1180.1(d) suggests that the presumption of harms in future mergers derives from two distinct threats: (1) transitional service disruptions that may temporarily negate shipper benefits; and (2) anticompetitive effects that are incapable of being identified and hence impossible to be directly mitigated through appropriate specific conditions. Neither of these concerns justifies a presumption against mergers because each can be dealt with in the context of any particular proposed merger, where each potential harm can be evaluated alongside potential benefits.

These potential harms are invalid bases for an antimerger bias for other reasons as well. The presumption that temporary service failures are inevitable is no doubt derived from the unfortunate experience of certain past mergers where the integration of rail systems resulted in well-documented problems. The proposed rules take important steps toward directly dealing with those potential

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5 *UP/SP*, Finance Docket No. 32760 (Sub-No. 21), Decision No. 16, served Dec. 15, 2000.

problems, and past problems have provided carriers with important knowledge of how to avoid these mishaps in the future. Assuming, nonetheless, that some amount of service problems could still occur in future integrations, the proposed rules presume potential harm sufficiently severe and protracted as to block approval of a merger on this basis. As a counterweight to this presumption, the proposed rules call for imposition of unrelated competitive enhancements. As demonstrated below and in the appended verified statement of Dr. Robert D. Willig, such regulatory impositions will foster inefficiency and unfairly and improperly saddle future rail operations on a permanent basis for what are, at worst, likely to be temporary potential harms.[6] Furthermore, it will be virtually impossible to predict the amount of permanently inefficient structural change to counterbalance this presumed temporary service setback or onto whose shoulders the presumed harm will fall. All the better that the Board leave such potential harm — if it materializes despite the enhanced emphasis on integration planning and service assurance contained in the Board's proposals — to the parties involved and their business negotiations and contractual, insurance and judicial or extrajudicial processes and remedies.

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[6] Even a merger whose implementation difficulties required service orders to be issued by the Board ultimately resulted in corrected service without raising further competitive problems. *See UP/SP*, Oversight Decision No. 16 at 2-3.

The second claimed threat that supports the Board's presumption, incurable competitive harm, similarly is insufficient basis for a presumption against future mergers. The Board's proposed rules fail to articulate any basis in fact or theory for its assumption that there are unremediable anticompetitive effects that will occur if any future Class I mergers are consummated. Nor have there been any comments filed by any party that identify specific unremediable problems that prospective Class I mergers present. In lieu of the Board's invoking such a presumption without factual basis, CSX has proffered that the Board should do as its sister agencies reviewing mergers do, and evaluate the competitive effects of each proposed merger on its own merits. CSX Opening Comments at 25-29. No other federal agency reviewing mergers sets up presumptions that would bar mergers without regard to their likely competitive effects, and no commenter has claimed otherwise.

Another reason that a presumption of incurable anticompetitive effects in future Class I mergers is bad policy is that nearly all commenters that discussed likely further mergers foresaw the likelihood of end-to-end mergers.[7] End-to-end mergers avoid anticompetitive issues altogether. Furthermore, as demonstrated below, and in Dr. Willig's Verified Statement, end-to-end (or vertical) mergers

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[7] *See, e.g.*, NGFA Reply Comments at 3, ACC [CMA] Reply Comments at 3.

frequently present procompetitive features that tend to benefit shippers. It, therefore, would be perverse to impose on such mergers a presumption of unremediable anticompetitive effects. Moreover, doing so unduly enhances the cost of undertaking an acquisition because a presumption not based on fact or theory is inherently unquantifiable. This likely will cause applicants to have to guess at the amount of "unrelated competitive enhancements" necessary to gain regulatory approval[8] and will embolden unaffected interests to line up to seek regulatory spoils.[9]

The procompetitive effects of vertical mergers are broadly recognized both within the rail industry and more generally in other industries. As is discussed more thoroughly in Dr. Willig's Verified Statement, vertical mergers provide for extended hauls, which lower operating costs and can increase the speed of service. Willig V.S. ¶¶ 14, 29. These cost savings are generally passed through to shippers because when costs go down the effect of lowering prices maximizes railroad profits, *i.e.*, by lowering prices a railroad tends to increase the amount of its service that is consumed by shippers along its tracks. By increasing output, with lower costs, profits increase above what they were before the cost savings was realized. Willig V.S. ¶¶ 6, 34-36. In fact, the Board's Staff Study confirmed that average

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[8] CSX Opening Comments at 35-49.

[9] CSX Opening Comments at 49; CSX Reply Comments at 26-27.

rate levels have decreased as a consequence of efficiencies brought about by regulatory reform. As the study observes: ". . . nearly all of the productivity gains have been passed along to rail customers (and ultimately consumers) in the form of lower rates — evidence that, on the whole, the railroad industry clearly operates in a competitive environment." *Staff Study* at 2.

While a number of past mergers have achieved these efficiencies through elimination of redundancies where overlapping operations existed, it would be a mistake to ignore the positive effect on shippers that other cost reductions will have from end-to-end mergers. Efficiencies in expansion of less costly service offerings, such as longer hauls, have contributed to price reductions resulting from post-Staggers reforms (Willig V.S. ¶¶ 34-36) and likely will be among the chief benefits to shippers if an end-to-end merger were proposed. The Staff Study is consistent with this conclusion.

It is necessary, therefore, in evaluating the competitive effects of a proposed merger, to evaluate the benefits of longer hauls and other cost savings that history has shown are likely to be passed through to consumers, in competition with other rail and non-rail transportation alternatives, against any likely anticompetitive effects.[10] Presumptions should not be levied against this analysis because to do so

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[10] Many commenters have advocated that the Board should develop merger rules for Class I railroads that end their competition analysis at rail-to-rail issues, that is,

Footnote continued on next page

might very well penalize or even discourage procompetitive mergers that would benefit shippers. Willig V.S. ¶¶ 25-28. The Board's decision to remove its prior presumption in favor of mergers already raises the bar, but the Final Rules must not enable opponents to use the bar to deliver a fatal blow to the brow of pro-competitive mergers by means of an unjustified and unquantifiable presumption.

II. THE BOARD'S REASSESSMENT OF ITS MERGER RULES HAS LED SHIPPERS AND SHORTLINE RAILROADS TO CALL FOR BROAD REREGULATION AND THE CREATION OF A PROCESS FOR DOLING OUT REGULATORY SPOILS.

Most, if not all, shippers profess that they favor the Board's proposal for "enhanced competition." But no shippers favor the Board's version of it. A considerable number continue to call for comprehensive, industry-wide reregulation. Many others are only slightly less bold, proposing, in essence, that

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Footnote continued from previous page

that competition from other transportation modes is to be ignored. This approach is at odds with railroad reality; railroads face daily competition from trucks, barges and ships. It is also fundamentally at odds with the conclusions of the recent Staff Study which demonstrates that the rail industry competes with other modes. Staff Study at 2. The study makes clear that "all types of rail customers, and not just those with competitive transportation alternatives, must have received some portion of the rate reductions we have measured here." *Id.* at 3. *See* Willig V.S. at ¶ 39. Consistent with the study, the competitive impact from other transport modes has long been recognized in prior Board decisions. This was a basis of the ICC's decision in the *Burlington Northern/Santa Fe* case. Finance Docket No. 32549, served Aug. 23, 1995, 10 I.C.C.2d 661 (1995). The Board should similarly resist these calls now to throw out the evidence and roll back the clock to discredited regulatory management of the railroads.

the Board use its conditioning powers to re-regulate the rail industry one company at a time. Parts II.A and B of these Comments reply to these continued calls for reregulation. Like proposals for reregulation, the Board's unrelated "competitive enhancements" proposal threatens to impose an arbitrary and unworkable regulatory tax on otherwise efficient transactions. This threat is examined in Part II.C. CSX's position is summed up in Part II.C.4.

A. Many Shippers Continue to Call for Industry-Wide Reregulation

It has been suggested that the comments of CSX and other Class I railroads warning against reregulation through these proceedings amount to empty cries of "wolf." A group of coal shippers even accuses "the rail industry [of] repeatedly [claiming] that every proposed change in regulation constitutes 're-regulation.'" Committee to Improve American Coal Transportation ("IMPACT") Reply Comments at 26. CSX agrees that not every proposed change in regulation constitutes reregulation. But various proposals put forth by other commenters in this proceeding openly call for industry-wide reregulation, not purportedly modest changes in regulation.

The National Industrial Transportation League and the American Chemistry Council, in their reply comments, continue to urge the Board to implement what would amount to a general forced access regime. NITL cites with favor various forced access proposals made by other commenters and argues that these evidence the need for the Board to adopt industry-wide reciprocal switching and terminal trackage rights requirements. NITL at 12-13. The American Chemistry Council simply urges the Board to consider adopting many, if not all, of the same forced access proposals cited by NITL. ACC [CMA] Reply Comments at 3-4.

These shipper associations indeed are not alone in their quest for industry-wide reregulation. The U.S. Department of Transportation, for example, continues to encourage the Board "to require all carriers serving affected gateways, not just the merging railroads," to be subject to the its forced access proposal. DOT Reply Comments at 4. "Certain Coal Shippers," Otter Tail Power Company, *et al.*, euphemistically call for "greater competition" in the railroad industry generally. Otter Tail, *et al.*, Reply Comments at 6. The Dow Chemical Company similarly proposes that the concept of "enhanced competition" "be expanded to the entire rail industry." Dow Reply Comments at 6.

Identifying some of the bolder, more explicit proposals for industry-wide reregulation is useful not only because it demonstrates that CSX is not itself crying "wolf" when urging the Board not to allow reregulation through the merger rules. It also is useful because it helps to reveal that many of the more subtle proposals concerning merger conditions and unrelated "competitive enhancements" may amount to a reregulatory wolf in sheep's clothing trying to sneak in the backdoor.

B. Many Shippers Continue to Propose Reregulation Through the Backdoor of Merger Conditions.

The Board explicitly has rejected proposals to re-regulate the rail system broadly through merger conditions. In the NPR, the Board interpreted its governing statute as prohibiting the use of its "conditioning powers to impose through merger approvals a broad program of open access . . . ." NPR at 16. Accordingly, the Board has concluded that making such a "fundamental shift in policy" by adopting a reregulatory approach is "better left to Congress," if done at all. NPR at 17.

Despite the Board's unequivocal rejection, many proponents of reregulation refuse to relent. Their comments often seize upon the Board's brief treatment of "major existing gateways," NPR at 14, and urge the Board to expand this concept and transform it into an unbounded open interchange requirement. NITL continues to tout its proposal to "more broadly define" what is meant by the term "major gateway," and to ensure that interchanges remain open both "physically and economically." NITL Reply Comments at 13-14. The American Chemistry Council, IMPACT, and U.S. Department of Transportation, among others, also continue to endorse conditions requiring interchanges to remain "economically" open. ACC Reply Comments at 3; IMPACT Reply Comments at 15; DOT Reply Comments at 4.

CSX certainly is against proposals to expand the Board's "major gateway" measure into an unbounded forced access requirement, forcing the maintenance of every interchange point. The "Subscribing Coal Shippers," Western Coal Traffic League, *et al.*, say that CSX opposes suggestions of this ilk, because it "do[es] not want the Board to condition future rail mergers with any meaningful competition-enhancing or service failure compensation conditions." Western Coal Traffic League, *et al.*, Reply Comments at 6. That contention is false. CSX opposes an unbounded "open gateways" requirement because broad gateway requirements, just like those proposed by NITL, were at the core of the failed DT&I conditions. They created inefficiencies and subsidies. They harm — not enhance — competition.

As discussed in our Opening Comments, CSX does not oppose a rule that would require merger applicants to indicate how they will preserve the use of "major" gateways, provided that major gateways be defined as the "well-established" transcontinental gateways (East-West) and similar well-established gateways North-South. In addition, the movements to be preserved at these transcontinental and comparable North-South gateways must be (1) specific as to duration, commodity, route, origin, and destination, and (2) substantial, such that they both (a) afford both originating and terminating carriers a substantial portion of the overall haul and (b) were used heavily during the period prior to the filing of the Notice of Intent. CSX Opening Comments at 17-18. These limitations are necessary to prevent the resurrection of the DT&I conditions. Their application should be reviewed in the context of the particular transaction involved.

The second reason CSX opposes unbounded "open gateways" proposals is that they, like other comprehensive forced access proposals, ask the Board to commit in advance to burden all future merger applicants with specific, mandatory regulatory tolls. As discussed in its Reply Comments, CSX respectfully submits that the Board ought not legislate specific outcomes through this rulemaking. It ought to make clear that, when analyzing a merger application, the Board will make competition issues first among equals in its public interest consideration. CSX Reply Comments at 28-33.

The Board should not tolerate, even if a merger applicant was so ill-advised as to propose it, the resurrection of the "commercial closing" doctrine, that was another core element in the DT&I conditions. A number of shippers have, with a fair degree of frankness, argued for reintroduction of the "commercial closing" doctrine, including in some cases the "proportionality" requirement. These price-rigidifying devices — giving the merged carrier a perverse incentive to keep its through-rates high so that they will not benefit the proportionate rate it must allow the interchange connection — could sap a major competitive strength of end-to-end mergers. The Board should neither require nor tolerate them.

C. Like Proposals for Comprehensive Reregulation, the Board's Unrelated "Competitive Enhancements" Proposal Threatens To Impose an Arbitrary and Unworkable Regulatory Tax.

In its Opening and Reply Comments, CSX devoted significant attention to the Board's proposal to require merger applicants to make proposals for "enhanced competition" that are not related to any identifiable merger-induced harm. NPR at 12-13. Nonetheless, it seems appropriate to reexamine the issue of unrelated "competitive enhancements," in light of two recent STB actions, STB Staff's rate study and the Board's oversight decision in *UP/SP*.

1. Increased Rail Carrier Efficiency Is "Enhanced Competition"

CSX cautioned in its Opening Comments that the NPR could be read to suggest that the Board expects merger applicants' proposals for "enhanced competition" to include proposals to benefit competitors, whether they benefit competition or not. CSX Opening Comments at 29-30. This is so because the Board's commentary mentioned only various forms of forced access as examples of "enhanced competition." NPR at 13. Indeed, the comments submitted by shippers and shortlines, without exception, assume that "enhanced competition" equals forced access.

CSX contends that if the Board is to look for enhancements of competition resulting from the transaction as an important criterion, it must be looked for wherever it is found, and that increased rail carrier efficiency must be recognized as a competitive benefit. Increased rail carrier efficiency — including cost savings, service improvements, economies of scale, scope, and density, longer hauls, elimination of inefficient interchanges, more efficient movements over the connecting lines of the merging parties, *etc.* — decreases the cost of service on a per-unit basis, thereby creating powerful incentives and abilities to provide shippers with true competitive benefits, lower rates and increased service. *See* CSX Opening Comments at 30-35. Driving up the costs of rail service by undermining the economies of scale, scope and density can produce the chimera of more options but only at the expense of higher prices to shippers and consumers. To take an extreme example, placing ten new carriers on a segment of track would multiply the number of options but would not result in lower cost operations. Indeed, it would have the opposite effect. Rail infrastructure has inherent limitations in flexibility. And even where the infrastructure can accommodate a second carrier, distributing the limited economic benefits to a non-owner may have serious negative repercussions. Adding even a second carrier can have the same effect by disturbing the economies of scale, scope and density achieved by the incumbent carrier. The failure of the DT&I conditions has proved just that, and it would be shortsighted to think that the underlying economics of rail transport are somehow different now that time has passed since the passage of the Staggers Act.

The point that low-cost operations rather than a higher-cost multiplicity of options leads to lowers prices and higher productivity finds robust evidentiary support in the Board's Staff Study published last month. The productivity gains achieved by railroads between 1980 and 1998 are staggering: by 1998, "Class I railroads produced 50 percent more ton-miles using 61 percent fewer employees, 28 percent fewer locomotives, 38 percent fewer track miles, and 23 percent fewer freight cars in service." *Staff Study* at 4-5. According to the Study, these productivity gains, "nearly all of [which] have been passed along to rail customers (and ultimately consumers) in the form of lower rates," represent the "most important factor" responsible for the remarkable 45.3 percent decline in inflation-adjusted U.S. rail rates between 1984 and 1999. *Id.* at 2, 4, 1. These observations lend strong support to CSX's contention that the Board should welcome proposals for "enhanced competition" that rely extensively, even exclusively, on credible claims of increased rail carrier efficiency.

2. Requiring Unrelated "Competitive Enhancements" Would Put the Process Itself at Risk

The most problematic aspect of the Board's "enhanced competition" proposal is that enhancements would not need to be related to any identifiable merger-induced harm. The merger review process itself would be an immediate casualty of this policy, as it would devolve into a convoluted, awkward, and inefficient grab bag. This is so primarily because by its very nature there is no principled basis for the application of the proposal. The proposal would overturn the "existing situations" rule, a simple, principled decisional tool calling for the dismissal of attempts to gain regulatory handouts made by parties unaffected by the merger. *See* CSX Opening Comments at 36-43. To appreciate the importance of this rule to the merger review process, one need only look back a few weeks to when the Board released its most recent *UP/SP* oversight decision. There the Board, applying the sound principle of the "existing situations" rule, was able appropriately to dismiss summarily the request of the California Public Utilities Commission for a study of competition in I-5 corridor, simply because the competition in question "did not exist before the merger, and CPUC has not shown that there could be any merger-related harm in this corridor."[11] Replacing this doctrine with an open invitation to seek handouts invariably will lead to a tidal wave of requests to feed at the public trough and to explore issues unrelated to the merger.

None of the shipper or shortline comments has made a serious, let alone convincing, effort to address this very practical problem, which must be solved before the Board could begin to pick the "winners" and "losers" of the chase for regulatory spoils. PPL Generation, for instance, suggests that Congress has

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11 *UP/SP*, Finance Docket No. 32760 (Sub-No. 21), Decision No. 16 at 12 (served Dec. 15, 2000).

provided "helpful" guidance, by "clearly contemplat[ing] that the Board would order trackage rights in and near terminals, and reciprocal switching agreements, 'where such agreements are necessary to provide competitive rail service.' " PPL Reply Comments at 16. PPL admits, however, that in order to find this guidance helpful the Board would have to reverse *Midtec*, and to allow access "relief" to be granted even absent a likelihood of competitive harm. A group of coal shippers unsurprisingly argues that the winners should be shippers (1) in rail dependent markets that (2) are served by fewer than three rail carriers by (3) increasing the number of serving rail carriers to three if possible. IMPACT Reply Comments at 33. IMPACT's principles, however, are derived from a false premise, that the current level of competition in the rail industry is inadequate to provide a "balanced and sustainable rail transportation system." STB Staff's most recent rate study confirms just the opposite, "that, on the whole, the railroad industry clearly operates in a competitive environment." *Staff Study* at 2.

Untethered from past precedent and the Board's most useful decisional tool, merger review proceedings would become even lengthier, more populous and more complex than they are today. The Board should strive to shorten, not lengthen, the process through this rulemaking. As discussed in Part I, most commenters foresee only primarily end-to-end mergers, which present far fewer competitive concerns and perhaps even greater competitive benefits than horizontal mergers. The more quickly these efficiency-enhancing mergers are processed, the more quickly the rail industry and consumers can reap their promised benefits.

3. Requiring Unrelated "Competitive Enhancements" Would Have Counterproductive Economic Effects

The deregulation brought about by the Staggers Act, as few dispute, has generated significant, measurable public benefits. The current environment gives railroads the incentive and ability to compete aggressively with all competing transport modes through demand-based pricing, the offering of new services, and the pursuit of a more efficient rail network. As evidenced most recently by STB Staff's latest rail rate study, this competitive environment has generated substantial productivity gains. Furthermore, as recognized by the Board in its fourth annual *UP/SP* oversight decision, consolidation among rail carriers very often is the catalyst for the achievement of efficiencies and productivity gains. In that decision, the Board concluded that the UP/SP merger has produced "vigorous competition and improved service in the West." *UP/SP*, at 6.[12] In addition to the record evidence, the Board pointed to Staff's rate study as corroborative of this conclusion:

> This study shows that rail rates in the West continued to decline rather sharply during the period from 1996 to 1999 when this merger was

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[12] *See also* STB Press Release, Surface Transportation Board Issues Decision In Its 4th Annual "UP-SP" Oversight Proceedings, Finds No Competitive Problems Resulting From Merger (December 15, 2000).

> being implemented. In this 3-year period, western rail rates fell 9.0%, or 3.1% per year on an inflation-adjusted basis. . . . Rate decreases of this magnitude could not have been realized if the UP/SP and BNSF mergers had substantially decreased rail competition in the region.

Id. In other words, productivity gains, including those realized through mergers, have been the "most important factor responsible for the rail rate reductions" since 1980. *Staff Study* at 4.

While past rail mergers have conferred these benefits, and future rail mergers, especially vertical ones, may yet provide more, if those mergers are burdened by so-called "competitive enhancements" unrelated to likely merger harms, the regulatory burden likely will have the perverse impact of creating anticompetitive effects. As is discussed more fully in Dr. Willig's verified statement, the imposition of "competitive enhancements" in the form of forced access will tend to undermine railroad network efficiencies such as efficiencies of scale, scope and density, and other savings identified above. The loss of these savings will cause rail prices to rise in relation to premerger levels, not fall as they otherwise have been shown to do. *See Staff Study* at 2. Lost savings will lead to higher-cost service, which will lead in turn to higher prices. Even if a few shippers obtain lower prices in the short run through the forced access, the great majority of shippers will suffer. If prices rise to the point that other modes of transportation become attractive to shippers, further losses of traffic will occur. This kind of "cure" will bleed the incumbent railroad in ways akin to the DT&I conditions and the commercial closing doctrine.

Whatever the precise situation of the "favored" shipper, Dr. Willig's V.S. makes it clear that the costs heaped upon the incumbent (including opportunity costs) are real and will fall upon <u>other</u> customers. There is no free lunch. A regulatory favor bestowed on a favored shipper must be paid for by someone, and as Dr. Willig demonstrates, that "someone" is other shippers. Only because the "someone" is a dispersed, numerous group does the cost appear transparent, but it is real nonetheless.

In contrast to forced access, when access to a railroad's tracks makes economic sense to them, railroads have provided it. But railroads do not voluntarily provide access to their tracks unless it increases the efficiency of their system and its assets. *See* Willig V.S. at ¶¶ 21-22.[13]

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[13] Compelled access will also likely cause the Board to have to become involved in costly and complex evaluations of railroad costs to determine the "correct" access price. *Cf.* the litigation over trackage rights fees for CP "East of the Hudson," scheduled by the Board to be completed in a month, which wound up taking six months. *Conrail*, Finance Docket No. 33388 (Sub-No. 69), Decision No. 102, served Nov. 20, 1998; Decision No. 109, served Dec. 18, 1998; Decision No. 123, served May 20, 1999. At least one earlier trackage rights fee case took the better part of a decade. *See St. Louis S.W. Ry. Compensation — Trackage Rights*, 1 I.C.C.2d 776 (1984), 4 I.C.C.2d 668 (1988), 5 I.C.C.2d 525 (1989), 8 I.C.C.2d 80 (1991), 8 I.C.C.2d 213 (1991).

If unrelated "competitive enhancements" produce more options that are not as low cost as the prior ones, they will not enhance competition but will harm it. Coupled with an unquantifiable antimerger bias in the form of a presumption of unremediable anticompetitive effects and service problems, the well-intentioned but shortsighted use of unrelated "competitive enhancements" will undo the beneficial effects of deregulation, in which the Board and its predecessor have played a major role. The impact of such a policy will harm the very shipper and consumer beneficiaries it seeks to assist.

CSX believes that the Board should approach the subject of competition in this fashion: there should be no "presumption" that major rail mergers are either "bad" or "good," either "procompetitive" or "anticompetitive." In this context the Board need not, and should not, draw a distinction between the various forms which procompetitive mergers may take. They may be procompetitive because of efficiencies introduced, by extending the length of hauls or otherwise, which permit rail carriers to compete more effectively in the transportation marketplace. Or they could be procompetitive by introducing more effective rail-to-rail competition. The *UP/SP* transaction, as demonstrated by the Staff Study, was procompetitive, although it did not introduce new rail-to-rail competition; it was in considerable part end-to-end, and otherwise it replaced competition between UP and SP by competition between UP and BNSF. A set of Rules that would not have permitted the *UP/SP* merger would have prevented a substantially procompetitive merger. The Board should be inclusive, not exclusive, in analyzing procompetitive outcomes.

4. CSX's Position on Competition Restated

The Board is correct to remove the presumption in favor of mergers. A presumption against mergers, however, is unfounded and the Board's consequent "enhanced competition" proposal is not supportable. Permanent forced enhanced competition is no remedy for transitory service difficulties. Moreover, the issue of unremediable competitive problems is a logical absurdity; if problems are hypothesized but their source and nature cannot be demonstrated, they should not in fact be presumed to exist; if they can be demonstrated, they ought to be directly remediated. No one has demonstrated a practical or theoretical basis for the existence of a third path between those alternatives. That being so, there is no logical reason why the procompetitiveness engendered by increased transportation efficiencies is not as good as that engendered by additional rail-to-rail competition, particularly since the credentials for forced access as actually increasing competitiveness are flawed, and indeed the contrary result will flow from them. An inclusive view of what is in fact procompetitive should be the Board's standard.

III. THE PROPOSED RULES ENCOURAGE COMMUNICATION AND AGREEMENTS AMONG INTERESTED PARTIES AND THE BOARD SHOULD CONTINUE TO FOSTER THESE TYPES OF COOPERATION.

One common thread broadly woven throughout the proposed rules that has generally received kudos from commenters is the Board's encouragement of communication among parties and negotiation of agreements to resolve foreseeable potential problems that may arise in the merger context. The Board emphasized the usefulness of such cooperative approaches in the following proposed sections:

- 1180.1(e) **Labor Implementation**. ("The Board supports early notice and consultation between management and the various unions leading to negotiated implementing agreements.")
- 1180.1(f) **Environment and Safety**. ("We encourage negotiated agreements between railroad applicants and affected communities . . .") and
- 1180.1(h) **Service Assurance and Operational Monitoring**. ("We will require applicants to establish problem resolution teams and specific procedures for problem resolution to ensure that post-merger service problems, related claims issues, and other matters are properly addressed. Also we envision the establishment of a Service Council made up of shippers, railroads and other interested parties to provide an ongoing forum . . . .")

These steps not only make sound use of the Board's limited resources, but they tend to encourage the marketplace to allocate known risks. This reserves the Board's role as an arbiter for what one hopes will be narrow classes of contentions that elude the cooperative process and which require a referee. That this approach is favored by diverse interests is further evidenced by the attempts of groups not expressly included in these bodies to join them. Thus, several ports have sought inclusion in the Service Councils, as have a number of labor, shortline and passenger interests. In the last round of comments, CSX advocated the inclusion of shortline, passenger, and port representatives. Reply Comments at 87.[14] CSX also applauded the Board's attempt to replace the formal traditional approach to oversight with a more flexible and informal process. *Id.* at 84-87. These new structures are process-oriented rather than adversarial. Contractual arrangements have been the general mode of interaction between freight and passenger rail carriers, and to the extent the Board continues to follow that approach, the better off both types of carriers and the public interest will be. *See* Part VI, below.

The one area when the Board has seemed seriously to fall short of fully embracing this more cooperative and communicative approach is in the area of service assurance planning. There the Board has proposed a "snapshot" approach

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[14] Inclusion of labor representatives, if they wished to participate, would certainly not be opposed by CSX. *See* Part VIII, below.

in which the applicants are supposed to provide details and predictions of the effects of integration, taking into account presumably all of the competitive reactions of other rail networks, and other transport modes over time. As drafted, the proposed rules seem to contemplate that the applicants adhere fairly rigidly to the plan, as presented in the Application. No doubt there is broad support among various commenting constituencies that the applicants should be responsible for service failures, and the Board is fully justified in insisting that the applicants demonstrate that they have, indeed, carefully considered and planned effectively for the integration process. Given past experience with service problems, possible service failures may be sufficiently foreseeable that transportation agreements can be negotiated to address them just like other risks in the transaction. This desire for accountability is not served, however, by the snapshot approach in the Board's Service Assurance Planning proposed rule (Proposed § 1180.1(h)). As CSX has described in its earlier filings, transition and integration is a process not a snapshot. CSX Opening Comments at 50-57. The proposed service assurance rules should be amended to extend the Board's cooperative and communicative approach to service integration planning and to avoid a shortsighted, "snapshot" approach.

The proposed rules should be amended to make it plain that service integration planning and service assurance plans are part of a dynamic, and above all, managerial, process that does not require slavish adherence to original plans, nor regulatory approvals other than those inherent in the Operational Monitoring process.

It is absolutely critical that the Board not turn the complex and dynamic integration process into a regulatory morass by attempting to regulate railroad operations by demanding formal amendments and agency review of changes to the service integration plan. If the Board inadvertently imposes rigidity upon managerial flexibility; *e.g.*, requiring approval to add a train, change a blocking plan, increase or decrease locomotive power, change the use of a yard, *etc.*, the resulting inability to respond will have a devastating — and we are sure, unintended — result.

This is not to say that the Board, shippers and other parties will not have avenues to follow the carrier' progress and adjustments. Operational Monitoring ensures that the Board will have information in a form useful to it. Interaction with the Service Council will by its nature generate information in forms of relevance to its constituencies.

IV. THE BOARD'S PROPOSAL AS TO DOWNSTREAM EFFECTS IS ESSENTIALLY SOUND AND IF PROPERLY ADMINISTERED CAN SOLVE CERTAIN "UPSTREAM ISSUES.

A. Background

Shortly after the filing in December 1999 of the Notice of Intent of CN and BNSF to place their railroads under common control, the Board announced that pursuant to authority given it under the existing rules, it was suspending its "one case at a time" rule. The Board then stated that it would expect the applicants (and other parties) to submit evidence and discussion of the likely reactions by way of other transactions that might be precipitated by their proposal and the overall effect on the public interest as expressed in the statutory goals set forth in 49 U.S.C. § 10101. Finance Docket No. 33842, decision served Dec. 28, 1999, at 5 (corrected version).

By doing this, at that time the Board recognized that consolidations in the industry had come to the point where it was no longer reasonable for the Board to preserve the rule that the consequences of the mergers it authorized, in terms of a response in the form of other proposed mergers, could rationally be ignored in evaluating a merger that might lead to such a response.[15] This realization that the Board should take into account additional major transactions that might follow its merger authorizations was broadly applauded by parties participating in the March 2000 hearings in *Ex Parte* No. 582.

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[15] The Board's perception, that one merger could lead to another, while correct and progressive, was supported by ample evidence of history and so was not a bold step into the unknown. Quite clearly, the BN/Santa Fe transaction led to UP/SP as a response, and the reduction of the three major rail systems in the West to two made Conrail, the third system in the East, willing, despite its Pennsylvania-style poison pill, to accept a proposal of merger by CSX, which later let to the CSX/NS Conrail transaction.

B. The Board's Proposal

Proposed § 1180.1(i) makes permanent the demise of the "one case at a time" rule as far as major merger cases are concerned. It imposes what CSX believes to be intended to be a modest and realistic requirement on applicants to furnish the Board with an indication of what they believe will be the reaction of the other major carriers to their action.[16] Surely two carriers that agree to a multi-billion dollar combination in an industry where there are only six very large participants, whose territory and operations are well known, would have done some advance thinking on what the reaction of the other major players would be and what the impact that reaction would have on their own combined operations.

So the Board has expressed the modest expectation that applicants, in their application, will "anticipate with as much certainty as possible what additional Class I merger applications are likely to be filed in response to their own application." The Board further asks them to explain their views on how those applications (if granted) could affect the eventual structure of the industry and the public interest. And some assessment of the effect on the benefits of the transaction by those further possible transactions is to be made, as is an estimate of what effect those transactions might have on the conditions that the applicants are

[16] It goes without saying that such a response may well be procompetitive, either *in toto* or in general.

proposing on their transaction, together with an estimate of what conditions might be required to be imposed on their own transaction if such further transactions in fact took place. The focus is strongly on the relationship between transactions and on judgments concerning appropriate conditions. Such a focus means that the Board could have greater confidence that any remediation that proves to be necessary in the first transaction is likely to remain effective within the context of major transactions that are likely to follow.

The obvious purposes of the proposal, besides the emphasis on correctly tailoring conditions, include, among other things, first, to increase the knowledge of the Board as to the likely consequences of its actions; and second, to prevent a sort of race to the Secretary's Office by parties who might hope to escape any remediation of the cumulative effects of their own transaction collectively with transactions that follow it, by simply filing first. A rule that the latter parties to file a merger application must themselves remediate any cumulative problems caused by their immediate predecessors and themselves, while the first to file may ignore cumulative effects, causes a sort of inappropriate regulatory bias in favor of filing early rather than later. While it might not strongly influence early filing, it would unfairly reward it. Given the present structure of the industry, a "first to file wins" rule does not seem an appropriate way to allocate the burden of remediation of whatever cumulative competitive problems may exist. The Board's proposal thus puts all industry participants on as level a playing field as possible, and, fulfilling the goal sought by CSX and others, can bring it about that parties who consummate a merger transaction will be given a clear view of the conditions that are to be imposed on their merger.

C. The Critics and Their Misconceptions

This modest proposal by the Board to substitute a degree of enlightenment in lieu of deliberate ignorance has caused a somewhat excessive reaction on the part of a number of interests that should know better. In particular, the proposal is viewed by CN with great fear and loathing; essentially CN wants the old rule of ignoring what comes next left in place. To counteract the "know-nothing" appearance of this, in a proposal that we cannot assume is serious, CN suggests that the Board occupy itself with a "workshop," or "seminar," on the pros and cons of having a continent-wide rail duopoly. No decisions would come from the workshop. This seminar or workshop would meet while individual mergers are processed as if each was a freestanding, unique occurrence without ancestors or descendants. CN also suggests that if the Board's proposed rule is adopted, it will (if it is an applicant, as most of CN's comments appear to contemplate) take the depositions of other major railroads to determine their own strategic plans, even though they have not filed a notice of intent or merger application, apparently in an attempt to create a distraction.

CN's complete aversion to looking at downstream effects (except to harass nonapplicants) is unique; but others propose a partial blindfold, and say that only other mergers that have been announced or have been the subject of a Notice of Intent[17] should be considered. Some cite the fact that the topic is somewhat speculative and so that it cannot be addressed with certainty, as if that were reason for doing nothing (and as if other estimates in merger applications were certainties).

These objections ignore the realities of the current major railroad structure in North America and misstate the proposals and interests of the Board. The fact is that there are only six major railroads left on the North American continent.[18] Certain particular couplings of their rail enterprises by those six are not presently in the common wisdom considered likely. And by definition, the filing of a Notice of Intent by two of the six will negate other possible combinations as long as that Notice is on the table.

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17 The two alternatives are essentially the same since Notices of Intent historically have been filed only a few days after public announcement.

18 While there is one additional Class I railroad in the Untied States that is not part of a system with those six railroads, and while one or more other railroads could become a Class I railroad in the future, if the proponents of a combination that did not involve two of the "Big Six" carriers could demonstrate by Petition that there was no reason to apply Proposed § 1180.1(i) to it, presumably after comment, the Board could grant a waiver if appropriate under the circumstances.

The task of analysis is not as great as the commenters claim, given the small numbers involved; there will be few additional realistic possibilities left once a single proposed coupling has been announced. The purpose of the exercise is not to determine whether those other reasonably likely combinations would be consistent with the public interest, but whether some special circumstances (whether positive or negative) raised by the proposed transaction in combination with one or more of the other reasonably likely transactions should be faced and anticipated in the first proceeding.

For its part, UP does not want a seminar or a workshop — it wants a trial to be held, in the first major merger case under the new rules, as to whether the devolution of the North American rail system into a continental duopoly of two major carriers would be in the public interest. That appears to be the only downstream effect that UP would have the Board examine — not the interaction between two mergers, one proposed and one which is a reasonably likely response. UP's view ignores the most fruitful use of examining downstream effects, the possible interactions between rail mergers. It also ignores the fact that the general question of further consolidation in the industry is what is at issue in the present rulemaking proceeding, and once this proceeding is concluded, the general parameters of evaluation of further major rail mergers that may be proposed will have been established. The question whether combinations between any of the six major railroads on the North American continent will be permitted (or, indeed, whether any will be proposed) [19] is one which will largely be determined by the outcome of the present rulemaking proceeding. If further mergers are proposed come June 2001 or thereafter, it will be time to evaluate them. They should be examined on their own merits, under the principles which CSX has supported in its comments, and with due regard to what the likely reaction or reactions by way of responsive transactions may reasonably be expected.

So the Board has it right again here. This proceeding will answer the policy questions, and individual cases will apply those policies. While cases will generally may be adjudicated one at a time,[20] they must be reviewed in a way that is fair and equitable to both the current applicants and those who may later file a proposal, <u>and</u> which permits the public interest to be served and not compromised by the relative timing of the transactions.

It cannot be denied that to some extent the process of considering the implications of "downstream effects" will involve a degree of speculation about

[19] Some commenters have, to be sure, made proposals to extract "merger taxes" so pervasive and costly that, if adopted, they would likely prevent all major mergers. *See* Parts I and II.

[20] Consolidation of concurrently pending proceedings need not be ruled out if there are multiple applications that are neither technically "responsive" nor "inconsistent" (which would lead to use of the standard procedure in such cases) but consolidation should not occur if it would unduly prolong the proceedings.

the future. But merger applications always contain projections about the future and this would be just one more. Just because something that is important to do cannot be done perfectly is no reason for not doing it at all. What may be anticipated as practical in the process contemplated by Proposed § 1180.1(i) is a fine-tuning of transactions and conditions. For example, if two transactions are authorized that would interact in a way that affected the public interest negatively, the necessary conditions to remediate that effect could be fairly allocated between the two combinations — obviously arranged not to take effect unless and until the assumed second transaction took place.[21]

Contrary to the assertions of some commenters, what the Board is proposing is not an exercise in state planning. The basic rules under which further Class I combinations will be determined are being worked out in this proceeding. The making of merger proposals will remain, as it has since 1940, in the hands of the free market, by ordering among private parties. The Board will remain in a reviewing mode. No proposal is being made for the adjudication, as to their consistency with the public interest, of mergers that have not been proposed. What would be examined is best viewed as a contingency; if <u>present</u> merger "X" is

[21] On the other hand, if a remedy that is imposed on the first transaction would not be necessary if a particular second transaction took place, provision could be made in the first transaction for an expedited removal of the condition upon the consummation of the second transaction.

consistent with the public interest, and a second likely merger "Y" following it is proposed and is found to be approvable generally as consistent with the public interest, is there something in the interaction of the two transactions that must be considered and dealt with so that the interaction of the two will not be adverse to the public interest? As the possibility of an "end-game" is presented, that the need for such a studied analysis of issues such as this becomes more pressing.

D. Relationship of Downstream Issues to Other Issues Involved in the Board's Adjudication of Major Mergers

This issue is closely related to the issue of the extent to which it is appropriate for the Board to exercise unfettered discretion in later applying merger conditions that were not anticipated at the time of approval of a transaction and its consummation. The Board's orders reserving jurisdiction, as CSX has observed (Reply Comments at 78), are generally broad and purport to set no limits on the sort of additional conditions the Board may impose. But to read orders literally would be, at best, of cloudy legality, and the Board itself has often, and most recently only last month, spoken out against retrospective application of conditions that could not be fairly foreseen at the time of approval of a transaction. *See Union Pacific Corp., et al. — Control and Merger — Southern Pacific Rail Corp., et al. — General Oversight*, Finance Docket No. 32760 (Sub-No. 21), served Dec. 15, 2000, at 12, where the Board rejected the notion of retroactively applying the proposed new merger guidelines to existing transactions, saying that the purpose of retaining oversight jurisdiction is "only to impose additional conditions where those that we have already imposed have proved inadequate to remedy competitive harms caused by the merger." In other words, there must have been a perception of a specific problem and an attempt at a specific solution, which solution was unavailing, if additional conditions are to be imposed on a consummated merger. It is clearly inappropriate for the Board to exercise an unfettered discretion to impose new conditions that were not contemplated in a transaction now consummated, whatever the generalities of the Board's reservation of jurisdiction may say.[22] The examination of downstream effects can resolve that problem and give the parties a clearer view of the contingencies that they face.

CSX's proposed touchstone of the appropriateness of an additional condition added after the consummation of a transaction is whether the applicants have been given fair warning of the specifics of the problems that might be addressed through later modifications or addition of conditions. CSX Reply Comments at 78-79. The provisions of Proposed § 1180.1(i), properly understood and administered, could solve problems of this sort; they are well-tailored to give parties involved in a first

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22 It bears focusing on just what a condition is: a burden that an applicant is required to undertake or satisfy if it decides to proceed to consummate a transaction. The transaction is approved on condition that the carrier abide by those conditions. The conditioning power is not a statutory license to the agency to require carriers that have recently merged to do additional things the agency thinks are good if not otherwise required by law.

transaction a fair indication of what adjustments might be involved were a certain other transaction or transactions to follow and be approved. As noted above, these adjustments might involve the loosening or termination of existing conditions as well as the imposition of new ones. As CSX's Reply Comments indicate, that would be a major advantage of the Board's proposal, not only to the Board, but also to the parties.

This discussion of the effect of subsequent transactions on transactions already consummated brings up the issue of "upstream" conditions, perceptively raised by Vice Chairman Burkes' separate comments. NPR at 40. Their view that "we need to look at the whole picture and not, with blinders on, look just forward" (*id.*) is well taken.

E. Impact on "Upstream" Issues

The proposed "downstream" rule also helps solve most of the "upstream" issues. The use of the conditioning power with "fair warning" of specific downstream contingencies under Proposed § 1180.1(i) solves the "upstream/downstream" dilemma identified by Vice Chairman Burkes with respect to pairs of transactions both occurring under the new rules. If, however, the conflict is between a transaction under the new rules and an existing transaction consummated under the prior rules, the issue of fairness and absence of retroactivity, well expressed in the Board's December 15, 2000, ruling in the

UP/SP oversight case, would be presented.[23] If the conflict is the one that Vice Chairman Burkes expresses, that the new transaction affects (and makes inadequate) a condition imposed in a prior transaction, and if there is some identity of the parties between the two transactions (as there would most likely be if one of the transactions were to affect the other), the problem could be resolved by imposing a condition on the transaction currently before the Board. And if the new transaction justified a loosening of a condition imposed on a prior transaction, issues as to fairness to the parties involved in the prior transaction would not be presented at all, and whether or not they were a party to the new transaction the Board would be free to loosen the condition, as it always would be, if it found that it would be in the public interest to do so.

The only situation where a difficulty would occur would be if there was a proposal to impose additional conditions on a consummated transaction that had been consummated under the old rules, where there was no identity of the parties, and where no fair notice of a specific change had been given in the prior transaction. In such a case, some other method of resolving such a situation would have to be found if a resolution of the issue was necessary to a finding of consistency with the public interest as to the second transaction.

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23 Finance Docket No. 32760 (Sub-No. 21), Decision No. 16, served Dec. 15, 2000, at 12.

The Board's proposal to take into account "downstream" transactions will, accordingly, make it easier to deal with "upstream" issues going forward.

To sum up: in CSX's view, the Board's Proposed § 1180.1(i) is well crafted, and if appropriately administered, could be of considerable benefit. We see in it no intent to create "state planning," and the parade of horribles conjured up by some commenters, for reasons related to their own strategies, are without merit. The Board should make plain the way in which it will administer the new rule in a way consistent with keeping unannounced transactions and explorations confidential.[24] With that observation, CSX supports it.

V. THE ATTACK ON THE BOARD'S TRANSBORDER PROPOSALS IS UNFOUNDED AND THE PROPOSALS ARE CONSISTENT WITH NAFTA.

In their filings commenting on the NPR and on the comments of others, CN and, to a lesser extent CP, continue their campaign, launched at the ANPR stage, to oppose the Board's efforts to gather important information related to transnational mergers and similar transactions. In an effort to give credibility to their claims,

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[24] It is, accordingly, fair to permit discovery of studies of possible responsive transactions made by applicants without permitting discovery of explorations made by non-applicant parties. The first tests assertions made by the applicants in the part of the application responsive to the new rules; the second has little or no relevance to the exploration of the issues, since the issue is whether the applicants' stated view as to what is reasonably likely is accurate — and not contradicted by their own studies.

CN and CP repeatedly cite NAFTA's policy objectives, and much less frequently cite actual NAFTA rules, as ostensible support for their position.

NAFTA thus serves as a purported basis for opposing the Board's efforts to gather information from foreign merger applicants on a wide range of issues. Questions about the ability of the foreign applicant to cooperate with U.S. regulatory bodies supposedly are off limits, as is the effect of legal restrictions or other constraints imposed on these companies' capacity to make undistorted commercial decisions. Questions related to restrictions on ownership and senior management, as well as U.S. national security concerns, are likewise dismissed as inconsistent with NAFTA.

However, common sense indicates that inquiries in these areas are important and eminently reasonable. As the U.S. Department of Transportation cogently observed in its Reply Comments dated December 18, 2000, at page 8,

> [The Board's proposals] serve the fundamental purpose of informing the STB about facts, laws, and policies that are important to an accurate and comprehensive understanding of major transactions.... In a combination involving only U.S. carriers, of course, the existence and application of relevant facts, law, and policy are either familiar or easily explored. That is not the case with transactions involving foreign-based railroads. Thus, without modification to its rules, the Board is in jeopardy of not knowing circumstances that can affect the public interests simply because they originate beyond our borders.
>
> To suggest that compiling a record in these cases is discriminatory or in violation of NAFTA is simply wrong.

DOT is absolutely correct. Indeed, a close reading of the CN and CP opening and reply comments reveals the utter flimsiness of their arguments. To begin with, in most instances, their only support for their arguments is a recital of what are said to be NAFTA's "objectives" as opposed to any citation of actual NAFTA rules that, in fact, would act as constraints on the Board's activity. Moreover, CN and CP's references to actual NAFTA provisions are provided with no context whatsoever. Accordingly, they misstate what the Treaty means and says. In fact, NAFTA gives the Board very broad powers to undertake precisely the inquiries to which CP and CN are objecting.

The details of CN's and CP's claims are reviewed below. Because CP's comments largely mirror CN's, the analysis that follows will largely speak in terms of the CN claims.

CN objects to four aspects of the Board's proposed regulations:[25]

- The requirement that non-U.S.-based merger participants explain how they will be able to cooperate fully with the Federal Railroad Administration; ("FRA")

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[25] There appears to be no objection to the "Full System" information requirements, CN and CP apparently realizing that not only are individual railroads "networks" but that they form networks with their connecting railroads despite national boundaries.

- The requirement that those applicants assess "the likelihood" that foreign provincial or national government policies, rather than strictly commercial concerns, could affect business decisions in a manner that was detrimental to U.S. transportation interests, including the interests of consumers of freight transportation services and the providers of such services;
- The requirement that those applicants discuss the potential that foreign government-imposed ownership restrictions might be factors relevant to the STB's assessment of whether the consolidation was in the public interest; and
- The requirement that applicants assess the U.S. national defense ramifications of their proposed mergers.

A. CN and CP Have No NAFTA Basis for Their Objections Concerning Investments and Investors.

CN claims that the proposed information requested by the Board violates NAFTA's antidiscrimination provisions, which it says require foreign "investors" and "service providers" to be treated the same as U.S. investors and providers. However, as noted above, CN fails to recognize which NAFTA rules actually apply here, and also misdefines the rules it erroneously says govern the STB's activities. In fact, the STB's actions comply with both the applicable NAFTA rules and the rules that CN erroneously cites.[26]

As CN and CP note, one subject of NAFTA engaged by the Merger rules is the subject of "investment" and "investors." Past history indicates that CN and CP are primarily concerned with whether the persons or entities who are stockholders in (and thus are investors in) CN or CP will be permitted to become investors in one of the U.S.-based carriers through a transaction in which such a carrier is acquired by, or merged into, CN or CP. That is vividly demonstrated by the aborted CN/BNSF transaction, which would have given the CN stockholders an interest in BNSF and the BNSF stockholders an interest in CN. But clearly there is no discrimination involved among investors in such a case involving either CN or CP.[27] It appears that most of CN's and most of CP's parents' stockholders are U.S. citizens, and thus both sets of investors, U.S. and Canadian, would be treated alike, regardless of what the specific Board regulations required with respect to the applications that CN or CP had to file. If future CN or CP initiatives mimic the past, there is no real need even to review CN and CP's complaints about proposed information requirements in future merger applications.

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[26] We provide the text of pertinent NAFTA Articles in an Attachment.

[27] Chapter 11 of NAFTA deals with discrimination against Canadian (or Mexican) investors vis-à-vis U.S. investors.

B. NAFTA Chapter Nine Gives the Board Broad Powers to Regulate in the Public Interest, Including the Power to Subject Non-U.S. Service Providers to Extra Burdens Where This Is Important to Achieving The Board's Legitimate Objectives.

While neither CP nor CN appears to be in a position to complain about NAFTA investor discrimination, it is still at least theoretically useful to analyze the situation that might be presented if somehow a purely Canadian or Mexican investor wanted to participate in a transnational merger involving a U.S. rail carrier.[28]

Even on that assumption, there is no basis for saying that the Board would overstep the bounds imposed by NAFTA in promulgating the information requirements in question. The objections raised by CN basically attack the level of protection of certain U.S. interests the Board is trying to achieve in the regulations it is proposing. However, the Board has ample support from NAFTA for the regulatory requirements it is proposing. The Board is charged with protecting the reliability, soundness and competitiveness of U.S. rail service, as well as the interest of U.S. consumers of freight rail services — the shippers and receivers of freight. The STB's proposed regulations reflect the STB's evaluation of the level

[28] CN also seeks to make an argument that Chapter 12 of NAFTA dealing with discrimination against Canadian (or Mexican) "service providers." We deal with that contention as well in this Section B.

of protection it wants to provide to minimize the risks of any damage to those objectives.

NAFTA Chapter 9, which outlines rules governing how government standards should be set when they affect other NAFTA countries, confirms the Board's full authority to assess the risks about which CN does not want to provide information, and its full authority to protect against those risks. NAFTA Chapter 9 preserves that authority despite whatever Chapter 11 or 12, NAFTA's investment and services chapters, might say. Therefore, CN's objections are without merit, even apart from the analysis in Section A, above.

NAFTA Chapter 9 outlines the rules governing the development, adoption, and maintenance by NAFTA governments of "standards-related measures . . . that may, directly or indirectly, affect trade in . . . services between the Parties," and of "measures of the Parties relating to such measures." (Article 901(1)).
Article 904(1) clarifies that each NAFTA government has the power to adopt standards-related measures, including any measure "relating to safety, the protection of human, animal or plant life or health, the environment or consumers," as well as "any measure to ensure its enforcement or implementation."
Article 904(1) also confirms that this standard-setting right includes the right to prohibit the provision of a service by an existing or proposed service provider of another party if the service fails to comply with the applicable standard measures

governing that service, or if a would-be service provider fails "to complete the Party's approval procedures."

- It is clear that the Board's evaluation of the "public interest" in determining whether a major rail combination should be approved, including its imposition of certain requirements complained of in the CN and CP submissions, is governed by the language of NAFTA Article 904(1):
- The issue concerning cooperation with the FRA obviously relates to "safety" and to "the protection of human . . . life." Those are goals of both the Board and the FRA.
- The requested discussion as to the likelihood that foreign provincial or national governmental policy will trump U.S. rail policy — based on the Staggers Act's concerns about competition and the "minimization of regulatory control" — clearly is related to the protection of "consumers." The consumers are the shippers and receivers of freight, whose protection was a major goal of both the Staggers Act and of the merger provisions in the statute. *See* 49 U.S.C. §§ 10101(1); 10101(4); and 11324(b)(1) and (5).
- The requirement of information concerning government-imposed ownership restrictions (and the expansion thereof to the Board of

Directors' nationality proposed by CSX) has a similar objective to that of the provision just mentioned.[29]

Article 904(2), read in conjunction with Article 907(2), confirms both that national regulatory bodies can exercise independent judgment concerning what level of protection they want to achieve, and that other NAFTA parties cannot second-guess this judgment.[30] Article 904(3) does incorporate Article 1202's broad obligations concerning nondiscriminatory treatment of foreign service providers into Chapter 9. However, Article 904(2) states that "[n]otwithstanding any other provision of this Chapter," each NAFTA government has the power to determine unilaterally the level of protection that it wants to provide in establishing regulations or standards designed to achieve "its legitimate objectives of safety or the protection of human, animal or plant life or health, the environment or consumers," as long as the determination is made in accordance with Article 907(2). In other words, Articles 904(2) and 907(2) override Article 904(3)

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29 As to the requirement to discuss the U.S. national defense ramifications of the transaction, CN cannot make even a superficial sort of NAFTA "discrimination" claim. See below, Section D.

30 NAFTA does not define "level of protection." However, a decision on the level of protection provided to achieve rail safety, for example, logically involves both a decision as to the types of risks to be protected against and a decision as to the intensity of protection the agency is trying to achieve. The STB's questions related to transnational mergers reflect a decision that adequate protection of the U.S. rail system requires a certain level of understanding of certain types of risks related to foreign legal, regulatory and political structures.

and fully insulate government decisions on the level of protection desired in a given policy area from the broad non-discrimination obligations otherwise applicable to NAFTA service providers.

Article 907(2) leaves no doubt in this regard, since it carefully spells out the level of deference given to the kinds of regulatory decisions described in Article 904(2). Article 907(2) states only that each NAFTA government "should avoid arbitrary or unjustifiable distinctions between similar . . . services in the level of protection it considers appropriate." (Emphasis added.) Importantly, Article 907(2) does not require a NAFTA government to avoid these types of distinctions. Rather, the NAFTA parties recognized that the complexities of national decision making concerning how much protection is adequate in policies affecting safety, consumer protection, health, and the environment make it inappropriate for national governments to be subjected to any type of mandatory restrictions on the protections they should accord.

Indeed, even the hortatory provision in Article 907(2) that a NAFTA government "should avoid arbitrary or unjustifiable distinctions" does not apply in every case. It only operates "where the distinctions:

"(a) result in arbitrary or unjustifiable discrimination against . . . service providers of another Party;

"(b) constitute a disguised restriction on trade between the Parties; or "(c) discriminate between similar . . . services for the same use under the same conditions that pose the same level of risk and provide similar benefits." Article 907(2).

In short, the NAFTA governments are urged only to try to avoid "arbitrary or unjustifiable distinctions," and even this effort is required in very limited circumstances.

Assuming (as we certainly would be justified in doing) that the Board is not trying to discriminate arbitrarily against Mexican or Canadian railroads, and that its actions are not a disguised trade restriction, the Board's obligations to try to avoid serious discrimination against foreign service providers apply only where the services provided by the domestic and foreign operations are functionally equivalent in all material respects. Foreign rail service providers wishing to make a major change in the structure of the U.S. rail system clearly do not qualify as providing services "under the same conditions" as U.S. based railroads, and their services do not "pose the same level of risk" as U.S. railroads, if for no other reason than the fact that they will be subject to two countries' rules and regulations, not just those of one country.

Furthermore, it is evident that the STB's questions are not unduly burdensome and are directly relevant to achieving the STB's legitimate objectives of assuring a safe, reliable and competitive rail system. Thus, a request that a foreign applicant demonstrate its capacity to cooperate with a U.S. regulatory authority charged with rail safety is directly related to the question whether the rail system will operate safely. When major rail operational decisions — let alone dispatching — and senior management decisions are being made in a foreign country, where the company will be subject to foreign government rules, the ability to cooperate clearly is a pertinent issue.

Similarly, asking a foreign rail service provider to discuss whether a foreign government's laws or other informal measures could distort the service provider's economic decisionmaking in a way that could create problems for U.S. shippers and other participants in the rail transportation network clearly is relevant to questions of the U.S. rail system's safety, reliability, and capacity to serve its consumers effectively. Moreover, despite CN's ardent protestations about the impossibility of such distortions occurring, the Port Authority of New York and New Jersey noted a concrete instance of precisely this kind of problem at page 5 of its Reply Comments. Within the past ten years, Canadian government authorities apparently have contemplated providing subsidies precisely to distort the normal economic decision making by Canadian railroads about how to route traffic to Canadian versus U.S. ports.

It is important for the Board to take this type of initiative into account, given its regulatory mandate, and it is only appropriate to ask the foreign railroads to step forward and provide information about these kinds of government actions. It is unrealistic to expect the Board or the foreign railroads' U.S. competitors even to be aware of all pertinent situations, while the foreign railroads living under the measures are in an excellent position to describe what is occurring.

Likewise, foreign government restrictions on ownership of a foreign corporation have the potential to create problems in the operation and management of the rail services, and it is perfectly legitimate for the STB to assure itself that it is protecting its legitimate public interest objectives by inquiring into these areas. Finally, it is obvious that the creation of a major foreign-based railroad providing important rail services in the United States could raise U.S. national defense issues.

Certain of the Board's proposed regulations also appear to qualify as "approval procedures" under NAFTA Chapter 9. Here again, the Board would be operating well within NAFTA's guidelines. NAFTA Article 915 defines an approval procedure as ". . . any . . . mandatory administrative procedure for granting permission for a . . . service to be produced, marketed or used for a stated purpose or under stated conditions." Article 908(3)(a) allows approval procedures to be applied as strictly as necessary to give the relevant agency "confidence that a . . . service conforms with an applicable technical regulation or standard, taking into account the risk that nonconformity would create."

Given the undeniable fact that in a transnational merger or consolidation, one of the merger elements would be subject to both U.S. and foreign government regulations, policies, and practices, it is entirely reasonable for the STB to ask precisely the questions CN is objecting to in deciding whether to approve the services that would be offered. The STB can and should ensure that its approval procedures are strict enough to give it adequate confidence that the risks to rail safety, reliability, consumer protection, and other important public values are kept at an acceptably low level.

As noted above, CN ignores the actual NAFTA rules governing the STB's proposed regulations and instead repeatedly refers to the fact that NAFTA contains provisions in Chapter 11 requiring nondiscriminatory treatment of Canadian and Mexican investors. However, in addition to the flaws in its analysis discussed in Section 3, below, CN fails to note that Article 1112 specifically states that provisions in other NAFTA Chapters are to prevail where they are inconsistent with NAFTA Chapter 11. Article 907(2)'s refusal to impose a mandatory anti-discrimination standard on agencies making risk assessments and decisions about the level of protection they wish to achieve clearly is inconsistent with Chapter 11's antidiscrimination requirements, just as it overrides the identical antidiscrimination rules in Chapter 12. Therefore, Chapter 11's rules must be read as overridden by those in Article 907(2).

C. Even if the NAFTA Rules Cited by CN Applied, They Would Not Support the NAFTA "Discrimination" Claim CN Attempts to Make.

Even if Article 1102's requirement of nondiscriminatory treatment of NAFTA investors, or NAFTA Article 1202's equivalent requirements with respect to NAFTA service providers were the governing standards, and even if Chapter 9 were not part of NAFTA, and even if all of the stockholders of CN or CP's parent were all Canadians instead of being mainly U.S. citizens, CN's arguments would still be wide of the mark. CN neglects to read the standards set forth in Article 1102 and Article 1202 closely enough to understand their true import. Specifically, both Article 1102 and Article 1202 require that NAFTA investors and service providers receive "treatment no less favorable" than what the U.S. accords to its own investors or service providers only when the foreign and U.S. investors or service providers are all operating "in like circumstances."

The Statement of Administrative Action accompanying the U.S. legislation implementing the North American Free Trade Agreement, which was formally approved by Congress, and thus is to be given great weight in interpreting NAFTA's provisions, discusses the "no less favorable treatment" standard in NAFTA and clearly establishes that the STB's actions do not violate this standard. The Statement of Administrative Action notes that the "no less favorable" standard

> does not require that service providers from other NAFTA countries receive the same or even 'equal' treatment as that provided to local companies or other foreign firms. Foreign service providers can be treated differently if circumstances warrant. For example, a state may impose special requirements on Canadian and Mexican service providers if necessary to protect consumers to the same degree as they are protected in respect of local firms. NAFTA's nondiscrimination provisions prohibit the imposition of laws and regulations designed to skew the terms of competition in favor of local firms; *they do not bar legitimate regulatory distinctions between such firms and foreign service providers*.

Statement of Administrative Action, House Doc. No. 103-159, Vol. 1, page 601 (emphasis supplied).

Common sense tells us that foreign-based rail service providers, with substantial operational and management control, as well as substantial equipment located in a foreign country are simply not in "like circumstances" with U.S.-based rail companies whose operations, management, and equipment are all located exclusively within the United States. This point is only reinforced when one considers the character of the STB's responsibilities. It is fully legitimate for the STB to be inquiring about the capacity of a foreign-based company (1) to cooperate with U.S. regulatory authorities, (2) to avoid problems with possible distortions created by foreign government policies or foreign government restrictions on corporate behavior or structure, and (3) to assess the defense risks created by cross-border services in such a sensitive area, given that the STB is charged with ensuring that it minimizes the risks of rail service disruptions, and protects rail safety as well as U.S. rail consumer interests.

Answering these questions is also not particularly onerous. Indeed, if the foreign rail service provider believes that it should be viewed as being, for all practical purposes, "in like circumstances" with U.S. rail service providers, it is far better positioned than the Board or others to bring forward information that will allay any concerns in this regard.

D. NAFTA Allows the U.S. to Take Any Actions It Considers Necessary to Protect Its Essential Security Interests.

Finally, CN does not even have a superficial basis to assert "discrimination" under NAFTA regarding the STB's proposed requirement that foreign merger applicants discuss the potential national defense ramifications of their merger applications. First, there is no formal difference whatsoever in the burdens imposed on CN or CP in this regard and those of U.S. applicants. Proposed § 1180.1(*l*) requires all applicants to, regardless of nationality, to discuss the transaction's effect on U.S. national defense issues. The fact that Proposed § 1180.11(c) apparently requires the same discussion from non-U.S.-based applicants means that Proposed § 1188.11(c) is surplusage, so there is not even a formal difference in filing burden.

Second, even if STB's new regulations were finally to include more extensive requests for national defense information from foreign applicants only, NAFTA Article 2102 explicitly permits each of the NAFTA governments to take any actions that they consider necessary "for the protection of their essential security interests." These security interests are defined to include "traffic and transactions in . . . goods, materials, services and technology undertaken directly or indirectly for the purpose of supplying a military or other security establishment." (NAFTA Article 2102(b)(i).) Accordingly, the STB is fully compliant with all NAFTA rules in making any inquiries it considers to be necessary to protect the U.S. national defense.

E. Conclusion

To sum up, CN and CP assert that the STB's proposed regulations unfairly increase the burden on foreign-based rail merger applicants to provide information to the STB, solely on the basis of the foreign nature of the applicant. However, this is an incorrect characterization of the situation. The STB has an obligation to ensure that a major rail consolidation is in the public interest of the United States, before that consolidation is approved and any changes in U.S. rail service occur. The STB likewise has the obligation to decide how it is going to meet its mandate and what inquiries it needs to make in order to reduce the risks of problems with a rail consolidation to an acceptable level.

Moreover, as a practical matter, CN and CP appear to be crying without being hurt. The requirements are not onerous, and CN and CP are the loudest in claiming that they would have nothing to fear from an examination of those issues the requirements seek to have ventilated. If the Board were to take a substantive action with respect to CN or CP or their stockholders which in fact violated NAFTA, CN or CP would not be without their remedies. The assumption that once this perfectly acceptable information is obtained by the Board, it will be used for some unlawful purpose is baseless. The fair treatment given by the Board and its predecessor over the years to the longstanding operations of the Canadian carriers in the U.S. makes such an assumption ridiculous.

The STB's requests for information from transnational merger applicants are designed to provide the Board with the assurance that it is adequately protecting the public interests it is required to defend. The STB has the obligation to ensure that the rail operations of foreign applicants will in fact have the critical characteristics and meet the operational requirements necessary to provide safe, reliable, and responsible rail transportation services in the United States. The STB's proposed regulations requiring transnational merger applicants to provide certain additional information related to their status as entities regulated by a foreign national or provincial government, in addition to whatever regulations U.S. authorities might impose, is a legitimate element in the set of protections the STB is trying to provide for the integrity and safe operation of the U.S. railway system. These requirements are fully consistent with and recognized by NAFTA.

VI. PASSENGER ISSUES

A. Reply Comments of Passenger Authorities Do Not Change the Right Answer.

Issues relating to passenger service are raised in the December filings of Amtrak, the Maryland Department of Transportation ("MDOT"), the Southern California Regional Rail Authority ("SCRRA"), and the United States Department of Transportation ("DOT"). Nothing in these filings undercuts CSX's comments regarding the appropriate handling of passenger issues presented in its November and December filings, and indeed Amtrak's filing supports CSX's position in important respects.

AMTRAK. On the positive side, Amtrak supports the view of CSX and other Class I railroads that applicants must have flexibility in implementing their Service Assurance Plans in order to adapt to changing circumstances. Amtrak Reply Comments at 3-4. Amtrak also acknowledges the important point that the fundamental relationship between freight railroads and passenger rail agencies is one of private contractual negotiation, not government regulation, and notes that it was able to protect its rights in the Conrail transaction without the Board's intervention. Amtrak Reply Comments at 5-6.

Paradoxically, however, Amtrak then also agrees with suggestions by commuter rail agencies that every existing passenger service should be considered an "essential service." Amtrak Reply Comments at 6-7. Amtrak's reliance on the

Board's grant of trackage rights to the New England Central Railroad ("NECR") in Conrail Decision No. 89 (served July 23, 1998, at 103-105) as support for this view is misplaced. There, the Board noted the potential adverse impacts to NECR's ability to host Amtrak service, but, in granting trackage rights, found that NECR would be financially harmed by the diversion of freight traffic and that "NECR provides important services both for its shippers and for Amtrak." *Id.* at 105 (emphasis added). The Board's grant of trackage rights to NECR was not premised on any presumption that all passenger services are essential services, and there has never been any legal basis for such a presumption in the Board's merger regulations. CSX endorses UP's presentation on passenger issues in its December 18 comments (at 30-32). In particular, CSX agrees with UP that, whether the Board decides to articulate its standard for analyzing impacts on passenger services as "harm to essential services" or as some other formulation, the substance of the matter is the same: the rule is (and the Board should make it clear) that the Board will not use the standard to add conflicting or inconsistent remedies to those provided in passenger service contracts and will not use the standard to require merging freight railroads to subsidize passenger service. Amtrak also endorses DOT's suggestion that the Board give passenger agencies more than the benefit of their contractual bargains with freight railroads by awarding them additional monetary remedies for service problems. Amtrak at 9-10. CSX strongly disagrees with both Amtrak and DOT regarding the proposed scheme to turn the Board into a claims tribunal for service mishaps, as explained fully in our December 18 filing. This proposal has little merit with respect to shippers, and has even less merit for passenger agencies, whose rights and obligations are defined by their contracts with the applicants.[31]

DOT. DOT supports Amtrak's suggestion that an application include pre-merger measures of on-time performance for passenger services. CSX similarly endorsed this suggestion in its December 18 filing.

MDOT AND SCRRA. In their similar filings, MDOT and SCRRA argue that applicants should be held inflexibly to the plans submitted with the application, or should be liable for monetary damages for deviations from those plans. MDOT and SCRRA also argue that the merger regulations should provide for an extremely broad scope of authority to impose new conditions during the oversight period. CSX and the other Class I carriers argued against these views in their prior comments (*see* Part IV.D, above and CSX's Reply Comments, Part IX). The

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[31] As explained in CSX's December 18 filing, CSX does not believe that the merger regulations should provide any presumption that the implementation of a merger be staged in any particular way (contrary to Amtrak's statement at 9), does not believe that the Board's jurisdiction to impose additional conditions during the oversight period is unlimited (contrary to Amtrak's position at 10), and does not believe that employees of passenger railroads have any labor protection rights (consistent with Amtrak's position at 11).

passenger agencies have even less cause to invoke the Board's intervention than other parties affected by mergers because their rights and obligations are determined by their contracts with the applicants, including incentives and penalties for service performance.

B. CSX's View Restated

In CSX's view, the fundamental position as to the relationship between passenger service and freight rail mergers, is this: in some cases passenger railroads operate on track and right-of-way owned (or held under long-term lease) by freight railroads, and in other cases freight railroads operate on track owned (or held under long-term leases) by passenger authorities. In these "interspecies" situations, the rights of the guest carrier to operate on the host carrier's lines are determined by contract (with certain statutory exceptions in the case of Amtrak); they are not subject to a regulatory regime but to private contracting,[32] as is most of the American economy.

The freight railroads and the passenger railroads have had, for a long time, contractual arrangements that contain the sort of assurances "across the board" that are now the subject of the Board's attention for use solely in the case of mergers. These very frequently include bonuses and penalties, individually negotiated and

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[32] Of course, in many areas other than the right to operate on the track of an owner, such as safety, a regulatory regime or regimes do apply.

often most creatively, with respect to the fulfillment of the promises that the host-railroad makes to the guest railroad. They are well established and do not need supplementation.

While clearly the impacts of mergers on existing passenger service is a subject that should be analyzed by the Board, there has been demonstrated no reason to change the fundamental contractual system that exists as a determinant of the relative rights of the host and guest. That system fairly allocates capital costs, permits an owning railroad to obtain revenues for use of otherwise unused capacity, and provides a basis for distinguishing situations where a guest carrier can rent the excess capacity of a host railroad and those cases where it will have to expect to bear its own capital costs for creating capacity to operate new or further service. Once again here there is a system which is not broke, and so there is no reason to fix it.

VII. SHORTLINE ISSUES

The Class II and III carriers, both individually and through their trade association, the American Short Line and Regional Railroad Association, have offered generalized, "wholesale" "solutions" to issues that need to be considered on a "retail," particularized basis. These carriers, from the smallest of shortlines through quite large regional carriers, such as Wisconsin Central on the cusp of becoming a Class I railroad, support a uniform "Bill of Rights" that would alter the basic private, negotiated bargains that were made in the connection with the creation of most of these carriers. The principal way in which these contracts are to be rewritten would be the wholesale termination of so-called "paper barriers" and "steel barriers." They would have this done either in connection with a merger or on a freestanding, across-the-board basis.

Few if any Class II or Class III carriers filed comments in the December 18 round; a set of comments by Wisconsin Central did not raise the usual Class II and III issues, but stressed WC's desire to remain a Class II carrier despite any growth in its revenues.[33] Accordingly, CSX stands on the comments which it filed earlier, particularly in Part V of its Reply Comments, pp. 42-51.

To summarize those comments: the elimination of so-called "paper barriers" and "steel barriers" is not a merger-related issue, and, on top of that, is substantively inappropriate, constituting an interference with private, negotiated contracts. The Board appropriately has treated shortline issues in merger cases on a "retail" basis, investigating whether there were issues in the particular merger

[33] WC proposes that in the event of further mergers, interests in jointly owned terminal and switching carriers ought to be divested, at least in part, by their owners, and made available to smaller carriers. WC Opening Comments at 5. Obviously WC has an eye on obtaining ownership interests in one or more of the jointly owned switching carriers in the Greater Chicago area. This proposal, which was also floated in the ANPR phase, is divorced from any showing of competitive necessity for divestiture and amounts to a simple grab attempt on the part of WC.

that inappropriately worked competitive or other cognizable harms on smaller carriers on the shippers located on them. The Board should continue that particularized, "retail" approach. Similarly, a blanket cloaking of each Class II and Class III carrier with the mantle of performing "essential services" is inappropriate and could, if implemented as requested by some commenters, exalt the preservation of individual competitors over the furthering of competition, and detract from the positive benefits of well-thought-out mergers. Again here, the issues need to be looked at on a "retail" basis.

A reasonable information requirement concerning the impacts their transaction will have on Class II and III carriers is certainly appropriate for imposition on applicants and such a measure should contribute to the particularized examination of impacts on smaller carriers that CSX favors. Such information requirements can lead to negotiated settlements that provide practical solutions rather than the application of across-the-board theories. Including shortline representatives on service councils could have the same beneficial effect of providing an opportunity for realistic, substantive dialogue rather than a litigative or forensic encounter. CSX urges the views it has expressed in the earlier rounds of comments with respect to smaller carriers.

VIII. ISSUES CONCERNING EMPLOYEES.

Reply comments on employee protection issues were submitted by the Department of Transportation ("DOT"), the Rail Labor Division of the Transportation Trades Department ("RLD"), and the Brotherhood of Railroad Signalmen ("BRS"). They repeat the same unsupported contentions that the Board should eliminate its process for modifying or overriding collective bargaining agreement obstacles to the implementation of the approved transaction or, alternatively, adopt a more restrictive necessity standard for modifying collective bargaining agreements. Like their earlier comments, they fail to show any legal or factual basis for altering the Board's existing employee protection standards.

A. Negotiations

As CSX explained in its reply comments, the Board should defer any consideration of requests to change the standards for modification of collective bargaining agreements until after the carriers and labor organizations have had the opportunity to renew efforts to reach a negotiated consensus, as the railroads have done with the United Transportation Union ("UTU"). As previously explained, several unions indicated in their comments a willingness to follow this approach.[34]

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[34] These unions were the Transportation Communications International Union, International Association of Machinists and Aerospace Workers International Union, International Brotherhood of Electrical Workers, and American Train Dispatchers Department of the Brotherhood of Locomotive Engineers.

In its reply comments, the BRS has now also agreed that the bargaining process between the National Carriers Conference Committee ("NCCC") and other unions "should continue," BRS Reply Comments at 2. CSX, however, does not agree with BRS's requests that the Board "return leverage to this process" by (1) setting a deadline before it issues "a final rule in this specific area" and (2) indicating that, absent a negotiated consensus within the deadline, the Board is considering a rule that prohibits an arbitrator acting as a delegee of the Board from modifying any collective bargaining agreement. CSX does not object to a requirement that the NCCC and involved unions report to the Board on the progress of renewed efforts to reach a broader consensus on employee protection issues, but establishing an arbitrary deadline would be counterproductive. Also, as previously explained in the comments of the National Railway Labor Conference ("NRLC") and individual carriers, there is no lawful basis for BRS's request that a rule be issued prohibiting changes to collective bargaining agreements.

B. No Basis to Adopt a More Restrictive Necessity Standard

In their Reply Comments, the Rail Labor Division and DOT continue to argue for a more restrictive necessity standard allegedly based on *City of*

Palestine v. United States, 559 F.2d 408 (5th Cir. 1977). However, they merely repeat their same unsupported rhetoric as the basis for their preferred standard.[35]

Their only proffered basis for adoption of a more stringent necessity standard is that, under the Board's existing necessity standard, the Board and its arbitrators have supposedly permitted the wholesale override of collective bargaining agreements merely for the sake of labor cost savings. DOT states that a more restrictive standard is necessary to "end the most egregious forms of wholesale contract overrides. . . ." DOT Reply Comments at 2. The Rail Labor Division identifies no specific instances where there was a wholesale override of agreements by "administrative fiat." For its part, DOT offers no independent analysis and merely mimics the unsupported allegations of the Rail Labor Division. Their contentions are clearly erroneous, as CSX explained in its Reply

[35] DOT continues to propose, in the alternative, that all labor issues relating to the implementation of a Board-approved consolidation be left to the bargaining processes of the Railway Labor Act ("RLA"), because, according to DOT, the relative size of the remaining large carriers gives them sufficient bargaining leverage with unions. DOT Reply Comments at 3. As the carriers have explained, this DOT proposal is foreclosed as a matter of law. In addition, DOT's reasoning is breathtaking in its naiveté. Under the RLA, unions have leverage not found in any other industry. Through the RLA status quo requirement, they can delay implementation of an approved consolidation indefinitely. Once released from the RLA's status quo requirement, an RLA union can engage in secondary picketing of any other carrier throughout the United States. It is precisely because the RLA does not provide for the peaceful resolution of labor disputes that the Board's governing statute requires that disputes over implementing agreements be resolved through arbitration and Board and judicial review.

Comments. For example, in the only specific supposedly "egregious" example of the use of the override authority cited by rail labor, the Fredenberger Award, the agreement modifications ultimately were not imposed by "administrative fiat," another overused and inaccurate phrase of labor and DOT. The unions' appeal of the Fredenberger Award led to a negotiated settlement between the involved carriers and unions.

In any event, the existing, judicially approved necessity standard already protects against the abuses imagined by rail labor and DOT. The Rail Labor Division barely acknowledges the existence of this necessity standard, which was enunciated by the D.C. Circuit in *Railway Labor Executives Ass'n v. United States*, 987 F.2d 806 (D.C. Cir. 1993) ("*Executives*"). DOT does not even mention it. The Board has adopted the *Executives* standard, holding, for example, in *Carmen III* that "the issue of necessity" has been "settled", citing *Executives* as well as *American Train Dispatchers Ass'n v. ICC*, 26 F.3d 1157, 1159-60 (D.C. Cir. 1994). *See Carmen III* at 21 n.20. Under this standard, as restated in *Carmen III*, collective bargaining agreement terms cannot be changed "willy-nilly." Modifications must be supported by "public transportation benefits." And, contract modifications cannot be justified solely by labor cost savings, as the Rail Labor Division continues erroneously to assert. 987 F.2d at 815.

Thus, the controlling necessity standard, as enunciated by the D.C. Circuit and adopted by the Board, already meets the legitimate concerns of rail labor, while ensuring that collective bargaining agreements will not frustrate realization of the benefits of approved railroad consolidations. In contrast, as explained in the Rebuttal Comments of the NRLC, the new necessity standard advocated by the Rail Labor Division and DOT, based on *City of Palestine*, is confusing, will lead to more litigation over an issue that is now settled, and, most importantly, will frustrate consolidations that have been found to be in the public interest.

Finally, the suggestion by the Rail Labor Division that the existing necessity standard is somehow arbitrary and capricious is feckless, given that the Board adopted the D.C. Circuit's standard. CSX also notes that no union sought further judicial review of *Executives*. Nor did any union appeal the Board's decision in *Carmen III*. The Rail Labor Division's last minute, inchoate musing that the current necessity standard "perhaps raises" Fifth Amendment issues also deserves no attention. RLD Reply Comments at 12. The Board and the courts have previously declined to consider union arguments based on asserted Fifth Amendment rights.[36]

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36 *See, e.g.*, *Executives*, 987 F.2d at 815.

C. No Basis for Other Changes in Employee Protective Conditions

The Rail Labor Division and DOT also fail to show any legal basis for changing existing protective conditions relating to relocation or test period averages.

Neither addresses the fact that any such changes cannot even be properly considered in this proceeding, because the Board gave no notice in the NPR to the railroad consolidation procedures that such changes were being proposed.

Nor does either commenter offer any basis for making changes in these areas. For example, to support the proposed change in the relocation requirement in the *New York Dock* conditions, DOT and Rail Labor Division rely on admittedly "hypothetical" scenarios, which have not been shown to have any basis in reality. If a transcontinental merger is proposed, the involved unions can propose a change in the relocation requirement for that merger. At that time, the Board would better be able to decide whether the proposed merger presents the "unusual circumstances" justifying a departure from its standard employee protective conditions.

Finally, DOT and UTU suggest that rail labor have a voice on the service councils proposed by the Board. DOT Reply Comments at 3. CSX has no objection to inclusion of rail labor on such councils.

In sum, the Board should modify Proposed Section 1180.1(e), as recommended by the carriers in the comments of the NRLC. Further, the Board should reject the proposals of rail labor and DOT to modify its employee protective conditions.

IX. THE VOTING TRUST PROPOSAL REVISITED

A. Background

With scant basis in the ANPR phase, the Board's NPR envisioned a radical change with respect to the Board's voting trust regulations, at least to the extent to which they apply to major rail combinations. *See* NPR at 25-26. The use of a voting trust to consummate the financial aspects of a transaction (the closing of a cash tender offer or the exchange of securities in a stock-for-stock transaction) prior to the Board's substantive approval of the transaction, to some limited extent places corporate transactions among railroads in the same playing field as those in other industries. Also, again to some limited extent, it provides a counterweight to what otherwise would be an enormous advantage of a hostile takeover of a railroad system by a party not involved in the rail transportation system over a transaction between railroads.

For several decades, the Board's and the ICC's rules have contemplated an informal procedure under which parties proposing to use a voting trust to effect the financial aspects of a transaction could proceed to do so on a schedule resembling that in other industries. The purpose of the use of a voting trust has been to shield the target of the acquisition from control by the acquiring entity during the process of the Board's review of the application. The rules have indicated in general terms the provisions that were expected in a voting trust agreement, and while there was no requirement of review by the Board's staff (or certainly by the Board itself), an informal staff review has been provided for. The sole issue in the review has been whether the agreement in fact effectively worked an isolation of the target from control by the acquiring company, and made appropriate provision for divestiture if the underlying transaction was not ultimately approved by the Board. This procedure has worked well over the years.

A single commenter in the ANPR process, the Port Authority of New York and New Jersey ("Port Authority"), sought change in the rules. Its concern was that effecting the delivery of the consideration for a transaction through a voting trust procedure made it difficult for the Board to turn down the transaction on its merits (despite the fact that the Board had turned down a major transaction after the institution of the voting trust rules in which a voting trust had in fact been used). In effect, the commenter felt, the Board committed itself to the transaction once the consideration was paid and the target's stock was put in the voting trust.[37]

[37] NY/NJ-2 at 14, filed May 16, 2000.

Concerns were expressed by the Port Authority that carriers might make a transaction that was financially unwise and which would leave them short of capital once the transaction was consummated, unable to make necessary capital improvements. The commenter did not get into details as to the text of a revision of the rules, but indicated that the Board itself was to decide whether to "approve" the voting trust after receiving "detailed financial information" to demonstrate that the surviving carrier would have sufficient financial strength "to make necessary investments in the ongoing rail operations." NY/NJ-2 at 14-15.

Apparently in response to this comment, the Board proposed in the NPR to make two changes in the voting trust rules: *First*, that review of the voting trust "up-front" was not to be even theoretically optional, but was to be required, and the review would be performed by the Board itself, rather than its staff. *Second*, the review would not be confined to the issue of whether unlawful control was adequately prevented by the voting trust arrangements, but would extend to deciding whether establishment of the voting trust was generally consistent with the public interest.

Because this change would have had grievous consequences for the use of a voting trust, a device which the Board had wisely sanctioned to put corporate participants in the railroad industry (at least to some extent) on the same level in effecting combinations as those in other industries, CSX filed extensive comments in the November 17 round, opposing the changes. CSX Opening Comments at 66-76. Other commenters did so as well.

B. The Advocate of Change Disappointed by the Board's Proposal

Interestingly enough, the voting trust proposal was another of the proposals in which the Board's apparently intended beneficiaries were not happy with the provisions that the Board had made for them.[38] The Port Authority filed reply comments rejecting the Board's proposal to analyze the voting trust agreement on a "consistency with the public interest" basis. The Port Authority acknowledged that the difficulties cited by CSX in this regard were real. Port of NY & NJ Reply Comments at 4. Instead, the Port Authority, while maintaining that the Board itself should make the review of the voting trust arrangements, proposed that the Board restrict its analysis so that it covered only (i) the prevention of unlawful control and (ii) the post-transaction maintenance of financial strength by the carriers involved in the voting trust in the light of the financial terms of the transaction.

C. CSX's Reaction

Adoption of the Port Authority's proposal does not, CSX believes, save the Board's proposal from the difficulties CSX (and indeed the Port Authority) perceived in the original NPR proposal. The issue of financial strength of the

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[38] The primary one was the unrelated competitive enhancements proposal. *See* CSX Reply Comments at 14-24.

carrier surviving a merger transaction cannot be resolved by a mere inspection of the financial terms of the transaction. As the Port Authority recognized in the ANPR phase, "detailed financial information" would be required. Indeed, that is an understatement; the inquiry would involve an analysis of much of the evidence that is characteristically submitted in applications to the Board. It involves the forecast of changes in intramodal and intermodal transportation that will accompany the transaction, and the financial effect of those changes on the surviving carrier; the major savings in expense to be realized in the transaction and the timing of that realization; the extent of capital improvements that will be needed, including their nature and location, by reason of changes in traffic patterns and increase in movements as a result of the transaction; and the nature of and costs and expenses related to the assurance of reliable service during the transition period. These calculations involve the development of the operational plans; the estimation of capacity of existing lines and facilities and the estimation of costs of additional track and facilities; the making of diversion studies with respect to other railroads and with respect to transportation by other modes; making an analysis of the quantum of overhead that can be eliminated; and the development and costing of service assurance plans. Endeavors of this sort would yield evidence that would form a major portion of the Board's analysis of the transaction on its merits.

But the problem with the Port Authority's present proposal is that the voting trust agreement is to be submitted for review, as it characteristically has been, at or about the time of the filing of the Notice of Intent.[39] While at that time the consideration to be paid in the transaction is generally known, the financial condition of the applicants upon the consummation of the transaction, and the needs of the combined carriers for financing, would not be definitively known at that time and certainly will not be known and demonstrable to the Board at that time. By definition there will be no application at that time, and indeed, absent waiver,[40] the application may not lawfully be filed for at least three months. So there will be before the Board no operating plan; no plan setting forth the details of the needs for capital improvements; no *pro forma* financial statements; no estimates of train counts; no studies of the amounts of merger savings; and no

39 In fact, the NPR contemplated that the voting trust agreement (if any) would be filed together with the Notice of Intent. The practice generally had been to file the voting trust agreement for comments and informal opinion by the staff within a few days after the filing of the Notice of Intent, in those cases where a voting trust was to be used. The point of using the voting trust is to permit the resolution of the financial issues in the market for corporate control without waiting the three months that must elapse before the application is to be filed with the Board, let alone the many additional months that will be required for the Board's analysis of the transaction and the rendition of its decision.

40 Only one such waiver has apparently ever been granted, that to CSX/NS in the Conrail case, and that only after separate CSX and NS Notices of Intent had been on file for about six months.

service assurance plans and, or course, no basis for costing the steps to be taken for giving assurance of a smooth integration.

The Board thus will be called upon to make a decision concerning financial strength without appropriate evidence in every major merger case using a voting trust. About all that the Board could do practically if it was required to make such a review at the outset in every major merger case ,would be summarily to approve voting trusts for stock-for-stock deals and treat deals involving cash as unproven, subjecting them to a lengthy more detailed review. But even that dichotomy, as well as being arbitrary, would be grossly wrong because the issuance of stock by a company that is an established dividend-payer involves a cash financial commitment of a real although not legally binding nature itself; and in many cases a cash transaction, which preserves a corporation's stock from dilution, can be a financially superior method of financing a corporate merger.

The same problems that CSX described and which the Port Authority acknowledged are accordingly presented in its current proposal: required substantive decision-making by the Board in all cases without evidence; the introduction of litigation into a process which has been developed over the years to the point where it is well-accepted judicially and essentially noncontroversial; judicial review of a premature decision made without adequate basis or backup; and invariable involvement by the Board in prejudging one of the statutory considerations that the Board is to consider in connection with every merger transaction, the financial aspect. *See* 49 U.S.C. § 11324(b)(3). The Port Authority's proposal is not a real compromise at all; it has the same vices as the Board's original proposal. The fact of the matter is that any attempt by the applicants to prove either general consistency with the public interest or consistency with a major aspect of the public interest, namely, the post-transaction financial soundness of the combined carriers, is fraught with procedural problems at the time contemplated by the Board's and the Port Authority's proposals.

D. The Board Retains Powers to Protect the Public Interest

The Board, however, is not without means to protect the public interest if a transaction within its jurisdiction is proposed which would clearly involve substantial financial risks and in which the consideration is to be delivered, through the use of a voting trust, prior to review by the Board. The Board could state that while in the ordinary case the use of a voting trust, with the standard provisions, including provisions for divestiture in the event of rejection of the transaction by the Board, enjoys the presumption of being both adequate to protect against unauthorized control and to ensure the financial stability of the combined carriers or, if the transaction is rejected on financial or any other grounds, sufficient to protect the carriers involved. The Board, however, might further provide that, for good cause shown, it could on its own motion or on Petition by an interested party suspend the effectiveness of the voting trust rules as to a proposed transaction and require applicants to make an appropriate preliminary showing as to financial matters, along the lines sought by the Port Authority in its comments. The adequacy and appropriateness of the voting trust would thus be presumed unless the Board determined to put a pertinent issue, whether of financial soundness or of protection from premature control, on the table for an advancer determination by the Board.

Under the existing rules, the Board's predecessor reserved and exercised the power to act through its own intervention as an exceptional matter in voting trust cases deserving special attention. The leading case is *Illinois Central Corp. — Common Control — Illinois Central Railroad Co. and Kansas City Southern Railway Co.*, ICC Finance Docket No. 32556, served Oct. 21, 1994. That case involved a unique "reverse" voting trust where Illinois Central Corporation, a railroad holding company for IC, proposed to put IC in a voting trust and acquire, and control, without a voting trust and without ICC authorization, KCS through acquisition of the latter's voting stock. The ICC took control of the voting trust process away from its staff and launched a proceeding to determine the consistency of the use of the reverse voting trust with the governing statute.[41]

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41 The ICC commenced its examination by inviting public comments, followed by reply comments by the applicants. The matter was never adjudicated on the

Footnote continued on next page

To be sure, a suspension of the voting trust rules and a related show-cause order would certainly result in delay in the employment of the particular voting trust and would require the submission of substantial evidence by the applicants if they wished to show cause why the suspension should be lifted. It would create a mini-trial of certain of the major issues in the case, in similar fashion to a resolution of a preliminary injunction motion in court. However, the proposal just suggested (unlike the Board's or the Port Authority's proposals) would not make an issue of the voting trust procedure in every case; presumably any suspension of the rules would be exceptional.

If the Board is of the view that a sort of safety valve needs to be maintained, the procedure just outlined by CSX could be followed. In the usual case, unless the Board determined that there is appropriate cause for a suspension of the rule

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Footnote continued from previous page
merits because the IC/KCS merger proposal was withdrawn shortly thereafter. For another exceptional interventions of the Board into voting trust issues, *see Union Pacific Corp. — Request for Informal Opinion — Voting Trust Agreement [Santa Fe]*, ICC Finance Docket No. 32619, served Dec. 20, 1994.

The IC/KCS voting trust was not employed by the parties, presumably out of concern that the Board would make a finding of unlawful control if the parties proceeded. While the case involving the Union Pacific and its proposed voting trust for the Santa Fe both involved only the issue of unauthorized control. Presumably applicants would not consummate a voting trust transaction if there was a serious threat of a finding of unauthorized control. In order to reserve its powers to suspend the voting trust provisions on the basis of broader concerns, such as financial soundness, the Board may wish expressly to include a provision for a power of suspension in its rules.

with a show-cause procedure by the applicants requesting dissolution of the suspension, there is no reason to involve the Board in review of the voting trust arrangements at all. In such ordinary cases an informal review, as to the conformity of the voting trust agreement with the rules, and with the insulation of the target from premature control, can be left in the hands of the staff. Given the fact that review by the Board's staff has historically been smoothly effected, there is no need to involve the Board in the review of voting trusts at all unless an issue of exceptional circumstances is recognized by the Board and the suspension procedure is invoked.

X. THE NEED FOR EXPEDITION

A number of the commenters have demonstrated that the Board's processing times for major rail mergers are considerably longer than merger review times for companies in other industries. This situation levies various tolls: the benefits of good mergers are postponed; the disruptions caused by a proposal to merge that is not in the public interest are prolonged; uncertainty continues to an undue extent; the personnel of the applicants and other rail carriers are distracted by the need to prepare and prosecute, or oppose, the application;; and concerns of employees at all levels as to the effect of the proposed transaction on them personally can fester.

Proposed § 1180.4(e) sets forth the statutory deadlines as the Rules' deadlines for processing merger applications. CSX believes that the purpose of the revision was simply to remove the outdated former statutory deadlines repealed in 1995 (which had been left in the Rules although contrary to the statute), and replace them by the new statutory deadlines contained in the ICC Termination Act. Certainly the Board does not intend that the statutory deadlines are a goal or a norm, rather than an extreme "outside" provision. CSX suggests that the Board might clarify that in its final rules.

CSX shares the views of BNSF and others with regard to the necessity of expediting the processing of merger applications as much as possible. While CSX believes that the schedule must be tailored to the particular merger before the Board, and does not endorse any "one size fits all" schedule (such as that put forward by BNSF), expedition is an important goal. Expedition should not be purchased, however, by sacrificing the procedural rights of those interests who respond to merger proposals, just as there should not be any additional procedures required as a toll for expedition. In this last regard, CSX notes the position taken by DOT (Reply Comments at 7-8) that applicants wishing to shorten the schedule should be required to take additional steps to ensure the participation of communities in the proceeding, including funding consultants to assist the communities or holding meetings in the communities. CSX would strongly oppose the Board's including such specific measures for community participation in the merger regulations. The Board's environmental regulations, as well as those of the

Council on Environmental Quality, provide sufficient guidance on compliance with the National Environmental Policy Act ("NEPA"), including appropriate measures to inform the public of the proposed federal action. The Board should not support such a proposal in its merger regulations.

Some commenters have urged that the Board aggressively inject itself into alliances and similar cooperative arrangements among the major railroads short of transactions that implicate 49 U.S.C. § 11323, and that proceedings to review those arrangements should be lengthy and protracted. CSX believes that there is no provision in the statute permitting the Board to expand its jurisdiction over alliances that meet neither terms of the merger statute, § 11323, or the pooling statute, § 11322, of Title 49 U.S.C. If not falling under those statutes and authorized by the Board thereunder, those alliances are subject to the antitrust laws.

Like end-to-end mergers, less integrative coordination between transportation providers, such as joint marketing arrangements, interline partnerships and other alliances, typically present far fewer concerns. They do not result in a permanent restructuring of the rail industry or threaten service disruptions that could inhibit the realization of the benefits flowing from coordination. Thus, to the extent such cooperative arrangements are subject to Board jurisdiction, the public interest best would be served if the Board were to make them subject to an exemption or an expedited process of review. Clearly the Board should not (indeed cannot) heed the calls from some commenters to attempt to regulate alliances that do not fall within its jurisdiction.[42]

CONCLUSION

When the Board issued its moratorium decision, it initiated the present project to reevaluate its merger rules, paying careful attention to the prospect of an endgame when mergers, encouraged by a promerger presumption might be announced in rapid succession. The proposed rules address this legitimate concern by removing the long-standing presumption in favor of mergers, requiring applicants to evaluate downstream effects, and where applicable, cross-border issues, as part of their initial filing.

If the Board properly applies its existing competitive analytical framework against this backdrop it will have achieved what it set out to do without undermining the ability of railroads to attempt to lower their costs and improve their service through consolidation. Thus far, the Board has successfully avoided the shortsighted calls of certain shippers and shortline interests that, under the mantra of "promoting competition" would replace markets with the same

[42] The issues of broadening the Board's jurisdiction or providing for procedural schedules in matters not involving major rail mergers do not, in any event, appear to be within the scope of the NPR.

regulatory judgments that were ensconced in the failed DT&I conditions and the commercial closing doctrine. Avoiding these calls makes good policy sense. As the Board's Staff rate study makes clear, the substitution of market-driven choices for regulatory judgments has resulted in enhanced competition and the win/win proposition of lower rates, improved service *and* financially healthier railroads. It is imperative for the Board to protect this legacy while making changes that improve its ability to distinguish potentially beneficial future Class I mergers from those that are anticompetitive. Thus, the Board should continue to resist these calls and should not reverse its presumption by adopting an antimerger bias.

A presumption against mergers itself will undermine many of the same benefits the Staff rate study identified, which were realized in part through consolidations. Similarly, the Board's proposed rule requiring "competitive enhancements" unrelated to merger harm threatens also to tax these same benefits. Such misnamed "enhancements" undermine efficient networks by introducing higher cost service which will provide only the chimera of more options while undermining the cost savings that allowed existing options to compete more effectively. The Board thus should protect competition, not individual competitors. In the end, mergers like competitors, should rise or fall on their merits. Ones that, on balance, benefit consumers should be approved and ones that do not should be fixed or denied. Only in this manner will the Board ensure that the benefits of competition of all types will continue to be passed on and that reliable rail service will continue to be available.

CSX accordingly respectfully asks the Board to consider and adopt its comments as contained in its Opening and Reply Comments and as summarized (and in some cases refined) herein.

Respectfully submitted.

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January 11, 2001

CERTIFICATE OF SERVICE

The undersigned counsel for CSX Corporation and CSX Transportation, Inc. hereby certifies that on this 11th day of January, 2001, a copy of the foregoing "Rebuttal Comments of CSX Corporation and CSX Transportation, Inc.," was served on all parties of record by first-class mail, postage prepaid, or more expedited method.

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ATTACHMENT

TO

REBUTTAL COMMENTS

OF

CSX CORPORATION AND
CSX TRANSPORTATION, INC.

PERTINENT NAFTA ARTICLES

ATTACHMENT

PERTINENT NAFTA ARTICLES

Article 901: Scope and Coverage

Article 901(1):

1. This Chapter applies to standards-related measures of a Party, other than those covered by Section B of Chapter Seven (Sanitary and Phytosanitary Measures), that may, directly or indirectly, affect trade in goods or services between the Parties, and to measures of the Parties relating to such measures. Article 904: Basic Rights and Obligations

Right to Take Standards-Related Measures

1. Each Party may, in accordance with this Agreement, adopt, maintain or apply any standards-related measure, including any such measure relating to safety, the protection of human, animal or plant life or health, the environment or consumers, and any measure to ensure its enforcement or implementation. Such measures include those to prohibit the importation of a good of another Party or the provision of a service by a service provider of another Party that fails to comply with the applicable requirements of those measures or to complete the Party's approval procedures.

Right to Establish Level of Protection

2. Notwithstanding any other provision of this Chapter, each Party may, in pursuing its legitimate objectives of safety or the protection of human, animal or plant life or health, the environment or consumers, establish the levels of protection that it considers appropriate in accordance with Article 907(2).
Non-Discriminatory Treatment

3. Each Party shall, in respect of its standards-related measures, accord to goods and service providers of another Party:

(a) national treatment in accordance with Article 301 (Market Access) or Article 1202 (Cross-Border Trade in Services); and

(b) treatment no less favorable than that it accords to like goods, or in like circumstances to service providers, of any other country.

Unnecessary Obstacles

4. No Party may prepare, adopt, maintain or apply any standards-related measure with a view to or with the effect of creating an unnecessary obstacle to trade between the Parties. An unnecessary obstacle to trade shall not be deemed to be created where:

(a) the demonstrable purpose of the measure is to achieve a legitimate objective; and

(b) the measure does not operate to exclude goods of another Party that meet that legitimate objective.

Article 907: Assessment of Risk

Article 907(2):

2. Where pursuant to Article 904(2) a Party establishes a level of protection that it considers appropriate and conducts an assessment of risk, it should avoid arbitrary or unjustifiable distinctions between similar goods or services in the level of protection it considers appropriate, where the distinctions:

(a) result in arbitrary or unjustifiable discrimination against goods or service providers of another Party;

(b) constitute a disguised restriction on trade between the Parties; or

(c) discriminate between similar goods or services for the same use under the same conditions that pose the same level of risk and provide similar benefits.

Article 1102: National Treatment

Article 1102(1):

1. Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

Article 1112: Relation to Other Chapters

Article 1112(1):

1. In the event of any inconsistency between this Chapter and another Chapter, the other Chapter shall prevail to the extent of the inconsistency.

Article 1202: National Treatment

Article 1202(1):

1. Each Party shall accord to service providers of another Party treatment no less favorable than that it accords, in like circumstances, to its own service providers.

APPENDIX

TO

REBUTTAL COMMENTS

OF

CSX CORPORATION AND
CSX TRANSPORTATION, INC.

VERIFIED STATEMENT

OF

DR. ROBERT D. WILLIG

Verified Statement of Robert D. Willig

Qualifications

1. I am currently Professor of Economics & Public Affairs at Princeton University and Faculty Chair of the Masters of Public Policy Program at Princeton University's Woodrow Wilson School. I earned a PhD in economics at Stanford University and subsequently served as Supervisor of Economic Research at Bell Laboratories. I served as Deputy Assistant Attorney General for Economics in the United States Department of Justice from 1989-1991 where, among other duties, I directed DOJ's economic analysis of mergers. I also participated in drafting the revised Merger *Guidelines* released jointly by the Department of Justice and the Federal Trade Commission in April 1992. I have served on various policy taskforces under the aegis of the Governor of New Jersey, the Defense Science Board, and the National Research Council.

2. I authored *Welfare Analysis of Policies Affecting Prices and Products.*; co-authored *Contestable Markets and the Theory of Industry Structure* (with William Baumol and John Panzar); and co-edited *The Handbook of Industrial Organization* (with Richard Schmalensee). I have written numerous articles, including "Merger Analysis, IO Theory, and Merger Guidelines," "Restructuring Regulation of the Railroad Industry" for the World Bank (with Ioannis Kessides), "Consumer's Surplus Without Apology," and "Free Entry and the Sustainability of Natural Monopoly." I am a fellow of the Econometric Society and have served on the editorial boards of the *American Economic Review,* the *Journal of Industrial Economics,* and *Utilities Policy.* My vita is attached as Exhibit RDW1.

3. I have previously provided statements and testimony on subjects relating to merger and regulatory policies before the Interstate Commerce Commission, the Surface Transportation Board, the Federal Energy Regulatory Commission, the Federal Trade Commission, the Federal Communications Commission, the Postal Rate Commission, the Public Utilities Commissions of many states, Federal and State courts in the U.S., and regulatory and judicial bodies all over the world. I have provided expert testimony in many antitrust cases, providing economic analyses of such pertinent subjects as competition, business combinations, market definition, entry, business practices, market power, and remedies for competitive concerns arising from mergers.

I. Introduction

4. The United States economy primarily relies upon markets to match buyers and sellers. Markets match individuals and firms seeking transportation services with other firms, including railroads, which supply these services. Firms, including railroads, *also* use markets to acquire the assets they use to produce goods and services. Productive assets range from individual locomotives and rail cars to entire lines-of-business or entire firms. Mergers are one way by which asset markets function to reallocate resources efficiently and productively.

5. Companies, including railroads, may merge or attempt to merge for a number of reasons. One possible reason of particular interest to competition authorities is that some firms might seek

to acquire especially troublesome rivals in order to remove a firm that has competitively constrained prices. The potential acquirer might hope to earn greater profits by, for example, raising price, reducing service, or both once the target firm disappears as an independent source of competition. Competition authorities in the United States and around the world seek to prevent this kind of anti-competitive merger from taking place.

6. However, it is critical to recognize that firms seeking to enhance their profitability by merging may also use mergers to reduce costs, to combine complementary assets, or to introduce more efficiently new or better products and services. When they are successful, such firms become more effective competitors—making business life more difficult for their rivals and benefiting consumers in the process. Merging firms that lower costs or provide new or better services *expect* both to attract more business by offering cheaper or better products *and* to become more profitable. This efficiency motive (or outcome) of a merger is usually viewed as desirable by nearly all competition authorities. Indeed, this is the "competitive enhancement" arising from a market for firms and for corporate control that should be the focus of merger analysis. When firms succeed in lowering cost and offering better or newer products, the firm and its customers and the general public interest all benefit.

7. Because the motives for mergers, as well as their outcomes, span the range from those that are privately profitable (for the merging parties) but harmful to consumers, to ones that benefit both the firms and their customers (or at least do not injure them), competition authorities cannot know in advance of careful analysis which type of merger they have before them. Hence, competition authorities should take the agnostic position of presuming only that firms intend to become more profitable through proposed mergers, while analyzing whether or not consumers and competition will be injured as a result. Mergers are market transactions, just like many others, and, as such, should be reviewed individually on their own merits, or lack of merits, from the perspective of the public interest in competition.

8. As discussed in the text below, I make four central points:

1. There should be no presumption in favor of or against Class I rail mergers;

2. Merger-related competitive remedies should be linked directly to merger-related competitive concerns;

3. The post-Staggers era, including the Board's past policies towards mergers, has led to marked productivity improvements that have been passed through in large part to shippers through lower rates; and

4. "Competitive enhancements" that are imposed rather than arising from the efficiencies flowing directly from a merger are very likely to be counter-productive and potentially anti-competitive.

II. Presumptions Make Bad Policy

9. Some mergers can and do raise significant competitive concerns. Not all mergers are efficient, or efficient in their entirety as proposed. For that reason, I support the Board's proposal to eliminate the decades-old presumption that mergers are generically desirable. However, I also strongly urge the Board *not* to change its historic approach to merger *analysis* by incorporating an inappropriate presumption that future mergers are generically likely to be *undesirable*. The appropriate approach to merger analysis is free of presumption regarding the merit or lack of merit of mergers. The Board's current approach to the competitive analysis of mergers based upon a careful analysis of the ultimate question – whether the merger at hand creates meaningful market power requiring government intervention – is sound and it is consistent with the approach to mergers taken by other Agencies with merger review authority. Eliminating the pro-merger presumption is a significant and important policy change that should not be undercut by putting in its place an anti-merger bias that has no theoretical or empirical support.

10. An anti-merger bias would threaten to impose regulation as a surrogate for market-driven choices. The corresponding imposition of so-called "competitive enhancements" (e.g., *involuntary* access) can perversely injure the shippers and consumers competition authorities normally seek to protect by imposing higher costs on railroads and on rail mergers, stultifying entrepreneurship, or even altogether deterring mergers that would have brought better pricing and better service to shippers and consumers. The Board recently noted that the UP-SP merger did *not* create "demonstrable competitive problems," and the Board "found no negative competitive effects stemming from the merger." More important, however, the Board concluded that "the UP-SP merger has produced *vigorous competition and improved service in the West.*"[1] Had this merger been "taxed" with extraneous "competitive enhancements" to unaffected regions or shippers, due to a presumptive bias against mergers, it might not have taken place. The customers who benefited from the "vigorous competition and improved service" the merger brought about would have been the losers.

11. As the Department of Transportation has noted:

> Shippers are not a homogeneous group and the freight transportation market is dynamic with changing customer requirements, new transportation opportunities, technological advances and interrelated services.[2] This characterization highlights the fact that railroad mergers and acquisitions may be a necessary avenue for efficiency and entrepreneurship in the dynamic freight transportation market. It also underscores the need to keep railroads free of stultifying regulation that is a response to an inappropriate presumption against mergers, rather than a cure for a particular competitive concern.

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1 Surface Transport Board, *Press Release*, December 15, 2000 (www.stb.dot.gov/newsrel.nsf/.../a8f0485edef04218852569b60055c946?OpenDocumen) and STB, *Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company—Control and Merger—Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and the Denver and Rio Grande Western Railroad Company*, Decision No. 16, December 13, 2000.

2 United States Department of Transportation, *Comprehensive TS&W Study*, 1997, Chapter 4, p. IV-1.

I2. Merger Related Remedies

12. In assessing the competitive issues in its public interest analysis, the Board's historical approach to mergers has appropriately focused on the market power arising specifically from a given merger. The Board's current practice is intended precisely to tailor remedies to prevent or ameliorate any identified increases in market power that are found to be likely results of a proposed merger. The Board has not sought to reregulate existing business relationships through the imposition of merger conditions not designed to remedy merger-specific competitive concerns. Neither has the Board sought to use merger review as a vehicle to address existing situations involving competitive issues with no apparent relationship to the merger itself. This approach is consistent with the general approaches taken by the Department of Justice ("DOJ"), the Federal Trade Commission ("FTC"), the Federal Energy Regulatory Commission ("FERC") and the Federal Communications Commission ("FCC"). As the Board's Fourth Report on the Union Pacific-Southern Pacific ("UP-SP") merger demonstrates, this approach has worked well.

13. The impacts of a proposed merger on inter-modal competition, efficient intra-modal competition and enhanced rail competitiveness (illustrated by generally declining real costs of rail service and improved service) should be the principal areas of focus of the Board's merger policy. Merger policy is *not* an appropriate vehicle for addressing issues and concerns that are not among the specific expected impacts of a proposed merger. If the Board grafts non-merger concerns onto merger review, the merger review process itself will become too cumbersome, time-consuming and costly. Each merger would then provide disaffected parties with an opportunity to raise issues that would require resolution before an otherwise beneficial merger—either as filed or as amended by the Board to resolve *merger-specific* concerns—could be implemented, thus delaying the merger's pro-competitive benefits to directly *affected* shippers.[3]

14. Linking Board approval of a merger to so-called "competitive enhancements" will make rail service less efficient. Perversely, the "competitive enhancement" proposal will predictably lead to inefficient, not efficient, access.[4] Railroads, just like every other business, have strong,

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3 It is well-known that the merger review process, even when it is confined to the specifics of the merger at hand, can be abused for anti-competitive ends. William Baumol & Janusz Ordover, "Antitrust: Source of Dynamic *and* Static Inefficiencies?," in Thomas Jorde and David Teece, eds., *Antitrust, Innovation, and Competitiveness* (Oxford University Press, 1992): 82-97. For example, a merger that makes two formerly weak competitors stronger may not be viewed positively by their remaining rivals. Second, a merger that reduces the costs of serving the merged-firms' customers may not be viewed positively by the customers' rivals. Parties who have not been directly affected by the merger may use any rights the Board accords them to insist that they, too, should "receive something," as much to delay or deny benefits to their commercial rivals as to obtain something efficient for themselves.

4 Future rail mergers are more likely than not to be primarily "end-to-end" (or "vertical") rather than mergers between railroads providing directly competitive parallel service (or "horizontal"). The term "vertical merger" most commonly means a merger between an input supplier and a customer, e.g., a locomotive supplier and a railroad. The parties to "vertical" mergers do not directly compete. Rather they complement one another. "End-to-end" mergers are quite similar. Indeed, one could view an "end-to-end" merger as a combination of firms that could reciprocally sell/buy service from one another. To complete an AB (Atlanta-Birmingham), BC (Birmingham-Corpus Cristi) movement (or the reverse), the AB railroad can be viewed as "selling" the AB movement to the BC railroad in order to allow it to complete the haul. Vertical or "end-to-end" mergers typically

profit-oriented, incentives to purchase services when and where they can do so more cheaply than they can provide the services internally. If a railroad can make better use of its valuable track assets, including "bottleneck" assets, other than by reserving them solely for its own use, it has the incentive to do so. It will do so in the interests of its own profitability. Hence, the analysis leads to the conclusion that when railroads do reserve their infrastructure for their own use, they are the most efficient—lowest cost—users of the right-of-way. The public interest is likely to be harmed by forced access arrangements that are viewed as "competitive enhancements," rather than as remedies for specific competitive concerns arising from a proposed merger.

I3. Post-Staggers Improvements to Rail Service

15. Most rail traffic faces competition from other modes, from other products, and from other geographic locations. Studies by academic economists, by the GAO and by this Board's Staff have all concluded that shippers' costs of moving traffic by rail have fallen since the Staggers Act was passed, whether rates are measured in revenue per ton mile or revenue per ton hauled. Finally, the sorry – indeed nearly disastrous – financial plight of U.S. railroads has been reversed. And this has been accomplished without the public subsidies provided railroads elsewhere in the world.[5]

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combine firms where each provides an input that complements—or makes more productive—an input or asset employed by the other firm. "End-to-end" mergers, for example, combine routes that permit a completed single-line long-haul, with the cost-savings associated with such a move. Moreover, primarily "end-to-end" mergers do *not* eliminate direct, parallel, competitors. "End-to-end" mergers allow firms to eliminate joint-rate setting and joint-responsibility for service quality and timeliness, and so more successfully compete against other railroads that may already offer single-line service and against other transportation modes, enhancing competition in the process.

While it is unlikely that a purely "end-to-end" merger would raise many competitive concerns, suppose that one did. Prior to a pending "end-to-end" merger, rail service customers conclude that *they* will pay higher rates or face reduced service quality as a result. Then these customers can, and undoubtedly will, make their complaints known to the Board. The Board has at least two options if it concludes that the complaint has merit. First, it can require the railroads to make the shipper whole by means of a remedy for the competitive problem. Second, if making the shipper whole is not feasible, the Board can weigh this specific competitive injury against the efficiencies likely to arise from the merger in its entirety and assess the merger on balance in terms of the "public interest" test.

Suppose a merger remains desirable for the affected merging parties, taking into account any remedies that are needed to protect affected shippers. Providing benefits—regulatory handouts—to *unaffected parties* makes it less likely that an otherwise desirable merger occurs. That policy choice will adversely affect shippers who would have benefited from otherwise pro-competitive mergers. Hence, the Board would become immersed inevitably in redistribution from one set of shippers to another, with a generally negative impact on efficiency and competitiveness.

5 For example, Norman Bonsor has noted with respect to Canadian transportation services that "government ownership and subsidy payments have been, and continue to be, a substantial burden on taxpayers." Bonsor, "Competition, Regulation, and Efficiency in the Canadian Railway and Highway Industries," The Fraser Institute (www.fraserinstitute.ca/publications/books/essays/chapter2.html). European railroad revenue covers as little as 20-25 percent of cost and in no case covers more than 80-85 percent. OECD, "Railways: Structure, Regulation and Competition Policy," DAFFE/CLP(98)1, Competition Policy Rountables, No. 15 (www.oecd.org/daf/clp/Roundtables/railw20.htm).

16. The Railroad Revitalization and Regulatory Reform Act ("4R Act," 1976), the Staggers Act (1980), and the Motor Carrier Act (1980) removed regulatory barriers to efficient use of transportation assets. Forced rate equalization and open routing, barriers to eliminating redundant capacity, implicit subsidies for specific types of traffic and geographic locations, and bans on confidential contracts had resulted in financial distress for the railroads, deteriorating service to shippers and declining use of rail to move freight. Perversely, the very restraints that were meant to preserve options for shippers actually promoted inefficient patterns of service, raised the cost of rail service needlessly, and prevented railroads and their customers from realizing lower costs and better service.[6] As a result of these inefficiencies, from 1950 to 1975, the rail share of shipped ton-miles declined by 19.5 percentage points, from 56.2 to 36.7 percent.[7] While rail freight traffic increased by 162 billion ton-miles between 1950 and 1975, had railroads maintained their 1950 traffic share, the increase would have been 564 billion ton-miles.[8]

17. The Board's recent Report[9] on rail rates confirms the earlier General Accounting Office ("GAO") study: rail rates in nominal and real terms have fallen since 1984 and since 1990, and the decline in rates cannot be ascribed to cost-shifting from railroads to shippers.[10] The Staggers Act, as implemented by the Interstate Commerce Commission and the Board, intentionally provided freedom to set rates efficiently with rates linked to both cost and demand – differential or Ramsey pricing – *and* provided for efficient rate ceilings for cases where a railroad arguably had market power. The rate structures that have emerged have been consistent with expectations. As the Board Staff and GAO Reports verify, revenue per ton and per ton-mile has fallen in real and nominal terms.

18. Alongside these regulatory changes, and the dynamic marketplace they helped create, went a series of Class I rail consolidations. These consolidations contributed to the overall gains in rail efficiency that drove prices down and rail ton-miles up. According to the DOT, "transportation efficiency has increased in recent years as a result of transportation industry

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6 Critics of current rail service ought to be reminded of the term "standing derailment," which gained currency in the 1970s. Railroad right-of-way was in such poor shape due to fiscal constraints that loaded railcars sometimes fell off track *while standing still* because the track gave way beneath them.

7 Of the various ways to measure the significance of a transportation mode, value of shipments, tons shipped, or ton-miles, the ton-mile metric favors railroads most. According to the 1997 Commodity Flow Survey, railroads accounted for 4.6 percent of value of shipments, 14 percent of tons shipped, and 38.4 percent of ton-miles. Trucks accounted for 71.7 percent of value of shipments, 69.4 percent of tons shipped, and 38.9 percent of ton-miles.

8 Transportation Policy Associates, *Transportation in America* (1983).

9 Office of Economics, Environmental Analysis, and Administration, December 15, 2000 ("Board's Staff Report").

10 Cost-shifting, when it does happen, occurs in the context of railroads and pipelines being the only transportation modes that own their infrastructure. To the extent that truck, water, or air carriers receive subsidies from tax revenue, costs have been broadly "shifted" from carriers to generic tax-payers.

consolidations, technological advances, and development of closer shipper/carrier/third-party relationships."[11]

I4. "Competitive Enhancements" Do Not Enhance Competition

19. Benefits that flowed from deregulation, described above, can be lost by regulatory imposition of forced access that does not make economic sense for railroads absent regulatory compulsion. Deregulation permitted railroads to end "rate equalization" and "open routing" practices that had resulted in a grossly uneconomic and inefficient rate structure and a proliferation of rates and routes that prevented realization of economies of traffic density and available economies of scale and scope. The "competitive enhancements" mentioned in the NPR do not address competitive concerns raised by a merger – they do not target remedies for market power over the shippers potentially at risk. Moreover, due to the Board's proposed adoption of a presumption of harm from a merger that is unknowable in terms of its extent or specificity, there does not appear to be any principled way by which to assess the extent of "competitive enhancements" of the sort mentioned in the NPR that would be sufficient for the authorization of a merger. Every shipper and every region will petition the Board for some share of the gains arising from a merger, regardless of how unobjectionable the merger would otherwise prove to be.

20. These predictable consequences of the NPR's proposed stance towards "competitive enhancements" raise serious and real concerns -- they might discourage what otherwise would be a merger that could create shipper and consumer benefits. Even if a railroad chose to offer up the requisite "competitive enhancements" as a cost of doing a merger—a "merger tax"--they actually promise to harm rather than enhance competition. When railroads choose, independently, not to grant some form of access, they likely do so because they do not foresee that doing so will permit them to expand profitably efficient service at the expense of their competition.

21. Railroads have historically from time-to-time exchanged rights to use each other's assets for a variety of reasons. Since such rights are generally long-lived, it is more important to consider the current "stock" of access rights rather than the number of new rights created, for example, each year. Some rights have been granted either in anticipation of or pursuant to Board approval of mergers. Other access rights have been granted as part of negotiations between shippers and railroads, as railroads compete for new freight business or to preserve existing business. Overhead has been granted when it efficiently allows a railroad to create or complete a single-line movement. Finally, local access has sometimes been granted where one railroad can more efficiently serve a customer than can the track owner, and this is typically done with some reciprocity.

22. Railroads do not voluntarily grant or exchange rights where the costs of service are likely to rise as a result. Imposition of forced access by regulation (even when one calls them "competitive enhancements") would serve only to lessen the ability of the rail assets to compete with other railroads and other transport modes. Compelled access would either be inefficient or it

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11 *1997 Comprehensive TW&W Study*, op cit., p. IV-2.

would be redundant, and in either case it would immerse the Board in complex and costly evaluations of railroad costs and the "correct" access price. Under a policy of compulsory access, some potential entrants will find it advantageous to put in claims for access even though they are not more efficient or as efficient as the incumbent or where their entry will cause adverse network impacts. If the Board bars their entry as inefficient, the Board's policy will mirror the marketplace and, hence, be redundant. On the other hand, if the Board's review process grants entry to inefficient suppliers or on inefficient terms, the "competitive enhancement" will reduce productivity and increase costs. The end result will be a movement in the direction of the pre-Staggers era where regulation preserved shipper options but ignored these same economic realities. The well-known result was service failure and railroad bankruptcy. The Board should allow market forces to continue to provide competitive benefits. The Board should use its merger review authority to evaluate mergers on their own individual merits by approving those that do not harm the public interest, fixing those that need to be fixed and can be fixed, and failing to approve the rest.

23. The remainder of my statement discusses these four issues in greater detail.

IIA. Merger Rules

24. The twin unifying themes behind modern competition analysis of mergers are, first, that mergers should not be permitted significantly to create or increase market power and, second, that many, although not all, mergers give rise to efficiencies. Sound merger analysis seeks to distinguish between mergers that on balance make consumers worse off from those that do not. While competition usually spurs firms to achieve efficiencies internally, efficiencies can also be realized through mergers via better utilization of existing assets. Efficiencies that arise from a merger can enhance the new firm's ability and incentive to compete, leading to lower costs, lower prices, more innovation, more investment, and better quality or new products or services. Of some importance in the case of railroads, mergers may permit two (or more) relatively ineffective (e.g., high cost or low quality) competitors to become more effective.

IIB. Presumptions Regarding the Ultimate Merits of Mergers Are Inconsistent with Sound Merger Analysis.

25. The Board has the power to approve Class I rail mergers "consistent with the public interest,"[12] a phrase naturally subject to some interpretation. One way to give this standard[13]

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[12] 49 USC ¶ 11324(c). Mergers that do not include a Class I railroad are governed by a less discretionary standard that focuses attention more directly on competitive effects. 49 USC ¶ 11324(d). Under the latter standard, the STB must approve a merger unless the Board finds that the transaction will have a substantial anti-competitive effect and that any anti-competitive consequences outweigh the public interest in meeting significant transportation needs.

[13] The statutory standard for evaluating rail mergers requires the Board to examine whether the merger has adverse effects on competition. 49 USC ¶¶ 11324(b)(1)-(5). A merger can produce adverse effects if it creates or

practical effect begins by recognizing that any horizontal merger may both create market power and various benefits going under the rubric of "efficiencies."[14] Merger analysis must, for the public interest, assess the likelihood that it will significantly increase market power,[15] as well as assess the likelihood it will produce important efficiencies. Consequently, the near 80-year

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enhances "market power." Normally, market power, or injury to competition, cannot and does not arise when the merging firms do not compete in the same market(s), or if efficiencies due to the merger make the merged firm a sufficiently more effective and efficient competitor.

A merger that augments or creates market power through unilateral effects typically results in a supplier's residual demand becoming less elastic, where "elasticity of demand" refers to the percentage change (e.g. reduction) in the quantity of the firm's output or service caused by a 1 percent change (e.g. increase) in price. Demand is "inelastic" when the percentage change in quantity is less than the percentage change in price, and demand is "elastic" otherwise. Market power relevant for merger analysis implies that a firm has, or comes to have, the power profitably to raise price above the competitive level and maintain it there. Sustainable long-run competitive prices allow the firm to recover the economic costs associated with providing its full range of services.

As a consequence of enhanced unilateral market power, *assuming no change in the supplier's marginal or incremental cost of supply*, the merged firm would have an incentive profitably to raise price by reducing its own output. Market power is unlikely to arise when merging firms face substantial competition from (a) suppliers of the same product or service located nearby, (b) suppliers of the same product or service located at a distance, (c) suppliers of different products or services, or (d) when entry or expansion by some or all of these suppliers is easy. Any of these market-driven reactions to the merged firm's attempt to increase price by reducing its own output or service level would cause price to remain at the pre-merger level by shifting sales to someone else. The only output level that falls is the merged firm's, making the attempt at price enhancement *unprofitable* to the firm that instigated it.

14 The classic reference to balancing market power against efficiencies is Oliver Williamson, ""Economies as an Antitrust Defense: The Welfare Tradeoffs," *American Economic Rev.*, vol. 68, March 1968: 18-34, with a correction in the *American Economic Rev.*, Vol. 69, December 1969: 954-959. For an example of a litigated non-transportation merger where market power claims by the government (Federal Trade Commission) were *unsuccessfully* rebutted by the defendant, see *FTC v. Staples & Office Depot*, 970 F. Supp. 1066 (D.D.C. 1997)(Hogan, J.). On the other hand, in *FTC v. H.J. Heinz & Beechnut*, (D.D.C. Oct. 18, 2000), No. 00-1688, the district court denied a preliminary injunction based, in part, upon the efficiencies likely to flow from the merger that would benefit consumers, although the number of competitors declined from three to two.

15 Market power creation is not synonymous with "rising prices". The point is obvious, especially in the context of American railroading, but often overlooked. When an industry declines cyclically or secularly the market process leads to prices that fail to cover forward looking total cost. This is a signal that capacity (resources generally) ought to be withdrawn to be used more productively elsewhere. One way to eliminate redundant resources is through a merger. This may be especially true when the industry involves networks or otherwise has production that occurs using complementary factors of production owned by different firms. By merging, the surviving entity may combine the most efficient elements of its predecessors and, so, continue to provide service as efficiently or more efficiently than before. However, as excess capacity is withdrawn, the price paid for the product or service rises toward a level consistent with recovery of total forward looking cost – the level consistent with competition. Prices persistently above total forward looking cost are undesirable. Prices forced artificially to remain below the level needed to cover the opportunity cost of the resources used are also undesirable. The value of the service being provided is less than the cost of providing it and, so, consumers are being subsidized to use too much. In a market economy (one without direct or indirect government subsidies), the consequence will be reduction in product quality or withdrawal of productive capacity as suppliers avoid uncompensated utilization of their resources.

presumption that railroad mergers are inherently "good" ought to be abandoned.[16] This would represent a significant and, in my opinion, welcome change. At the same time, the Board should strongly resist replacing this presumption with its opposite, namely that railroad mergers are inherently suspect or "bad."[17] This is especially so given the practical reality that subsequent mergers are likely to be end-to-end, or vertical, rather than mergers between direct horizontal competitors offering parallel service.

26. Any Agency reviewing mergers should take a presumption-free approach to the competitive merits of a specific merger. Presumptions regarding the ultimate question – whether a specific merger does or does not raise significant competitive concerns that rise to the level sufficient for governmental intervention– fundamentally interfere with careful analysis.[18] Economists and lawyers who have analyzed horizontal mergers in great detail over the past 30 years have come to understand how and why the elimination of a specific competitor through a merger may give rise to market power that injures consumers, or *less* frequently input suppliers by creating monopsony power. I urge the Surface Transportation Board ("the Board") not to adopt

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16 For examples of the pro-merger presumption associated with the perceived need to eliminate chronic excess capacity, see *Penn-Central & N&W Inclusion Cases*, 389 U.S. 486, 492 (1968) and *Lamoille Valley Railroad Co. v. I.C.C.*, 711 F.2d 295, 301 (D.C. Cir. 1983). The Transportation Act of 1920 directed the I.C.C. to prepare a plan to consolidate the railroads, and the I.C.C. formally adopted such a plan in 1929, though it was never put into effect.

17 As the Board correctly noted in its *General Oversight Decision* No. 10, slip op. at 5:

> We…agree with the assessment of the Department of Transportation (DOT) in its submission that "BNSF market share … should not be the decisive criterion by which the level of competition is judged. … [T]he most important indicator of the impact of the trackage rights conditions is the effect BNSF's presence in the market has on the rates offered by UPSP.

The proper analytical approach begins with the clearly articulated and practical goal of determining a merger's likely impact on rates paid by affected shippers. By relying upon "presumptions" of either the global kind – mergers are inherently "good" or "bad" – or the more narrow kind – market share determines the outcome – the analysis may well never reach the relevant issue: impact on competition.

18 The uses of the word "presumption" in the present context may be a source of confusion. There is a significant difference between "presuming" the answer to a question: Are mergers beneficial?; and structuring the analysis needed to arrive at that answer in a way that creates temporary *evidentiary* or *analytical* presumptions as part of an orderly process with shifting *burdens of proof*. The Merger Guidelines, for example, do not presume the ultimate answer. They do consistent with court and Agency practice, structure the analysis of specific mergers by the use of presumptions related to which party has the burden of persuasion. For example, the plaintiff (government) can establish a *preliminary* demonstration of likely anticompetitive effects by (1) articulating and defending a product market, (b) demonstrating that the merging firms are important competitors in that market (e.g., high market shares, evident competitive rivalry), (c) establishing barriers to entry and expansion, and (d) providing a plausible explanation as to how and why the post-merger incentives will lead the newly merged firm to raise price, reduce quality, or both. At this point the burden of proof shifts to the Parties and if they successfully rebut the plaintiff's case, then the *presumption* shifts in their favor—the merger is competitive benign. This is not, however, the apparent intent of the proposed Board merger revisions—simply to lay out a new *procedure* for analyzing mergers without any intention of changing the substantive outcome. Because the Merger Guidelines, articles written about them, or decisions arrived at using them, occasionally are articulated in terms of "presumptions", it is important to be clear that the Guidelines approach to "presumptions" and the Board's proposal are not the same.

a generic *ex ante* presumption regarding the merits of mergers. A general presumption as to the ultimate competitive consequence of mergers gives a merger-reviewer the appearance of having determined the outcome of a merger evaluation proceeding independent of the evidence and analysis presented. Each merger presents its own set of facts, and careful merger analysis must identify both potential competitive concerns as well as potential efficiencies, seek to determine the likelihood of each, and to assess their magnitudes. A policy of merger review based upon presumptions – a "thumb on the scale" approach – runs counter to careful analysis precisely because presumptions are not susceptible to measurement and are, hence, a source of discretion that would make the Board's resolution of mergers less transparent and less accurate to an extent that would be difficult to assess and control.

27. The Board and its predecessor, the Interstate Commerce Commission ("I.C.C."), have *presumed* that mergers are beneficial, especially if they helped eliminate arguably excess capacity. By eliminating this presumption, the Board will make a significant change in transportation policy, and I believe a desirable one.[19] There is support for the efficiency-enhancing potential of mergers among competition authorities in the United States. This is a widely shared belief by antitrust enforcement officials who have served at the Department of Justice and the Federal Trade Commission.[20] Hence, I believe it would be quite wrong for the Board to replace its previous

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19 Railroads have been eliminating redundant capacity for the past twenty years, while simultaneously investing in new and replacement capacity where it has been needed for new and continuing efficient service. Moreover, shipping patterns changed over that period of time as well. As a result, a pro-merger policy presumption predicated on the need to encourage capacity-rationalizing mergers is no longer appropriate.

20 The Federal Trade Commission has noted in its recent antitrust guide to the public:

> Most mergers *actually benefit competition and consumers* by allowing firms to operate more efficiently. But some are likely to lessen competition.

Federal Trade Commission, "Promoting Competition, Protecting Consumers: A Plain English Guide to Antitrust Laws," www.ftc.gov/bc/compguide/index.htm. (emphasis added).

Similarly, officials at the Department of Justice have made the same points in speeches and testimony. Former Deputy Assistant Attorney General Lawrence R. Fullerton highlighted both the analytical approach taken by the Department and the Federal Trade Commission as well as the generally benign consequences of most mergers:

> As these (Merger) Guidelines make clear, our review focuses on whether the merger would create or enhance market power, or facilitate its exercise. ...
>
> Our approach to horizontal merger analysis is first to define economically meaningful markets, along relevant product and geographic lines, assign market shares, and assess whether the merger would increase concentration significantly – to the point that post-merger concentration levels would be high.
>
> We then assess whether anticompetitive effects are likely, given these concentration levels and other characteristics of the market. ...
>
> There are three important points to emphasize about our application of these principles:
>
> 1. The Division only challenges mergers that hurt consumers – that is, hurts consumers by raising prices, or by reducing product output, quality, service or innovation. ... Our reviews of mergers are not driven by concerns about the market positions of particular competitors, or protecting existing supply relationships.

pro-merger stance with one that is fundamentally hostile to them. This is especially true in the case of "end-to-end" mergers that combine firms providing complementary rail services.[21]

28. By eschewing presumptions and, instead, setting out a clear analytical approach by which mergers may be evaluated, the Board provides transparency, predictability and accuracy. This approach has worked well.[22] It allows the Board, as well as affected parties, to understand,

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2. We recognize that the vast majority of mergers are competitively neutral or even beneficial for competition and consumers. This may be because they create synergies, improve or create new products, and/or lower costs. We recognize that vertical mergers, in particular, often create efficiencies. ...

3. For both of these reasons, we do not approach merger analysis mechanistically.

Deputy Ass't Attorney General Lawrence R. Fullerton, "Recent Developments in Merger Enforcement," Statement before The Conference Board Council of Chief Legal Officers, February 9, 1996 (www.usdoj.gov/atr/public/speeches/fullerton.txt). These comments are entirely consistent with my own views: mergers are not treated mechanistically or presumptively. Many mergers – especially most vertical mergers – do not raise competitive concerns, and asset transfers via merger may facilitate more efficient use of resources to benefit consumers. One of my successors as Deputy Assistant Attorney General for Economics, Prof. Carl Shapiro, has noted that "the vast majority of proposed mergers and acquisitions either raise no significant antitrust concerns, or ultimately pass muster after agency review. This is true in part because many mergers are not among actual or potential rivals. Many other deals are primarily vertical in nature, e.g., in the telecommunications sector, and vertical deals are far less likely to raise antitrust concerns than horizontal deals." Carl Shapiro, "Mergers with Differentiated Products," Address before the American Bar Association and International Bar Association, November 9, 1995. None of these officials referred to "presumptions" as part of a careful merger analysis.

21 Most important railroad mergers are likely to have both "parallel" and "end-to-end" elements. Hence, even if a hypothetical purely "end-to-end" merger were always deemed competitively desirable, the actual mergers the Board must review would still require a detailed analysis.

22 The process leading to this Board's authorization of the Union Pacific-Southern Pacific ("UP-SP") merger is an example of the way this approach has effectively protected consumers. When the UP-SP merger was first proposed, both the Department of Justice and the Department of Transportation, along with a number of states (e.g., Texas, Utah) raised concerns about both the underlying transaction as well as the Parties' proposed trackage rights agreement with the Burlington Northern/Santa Fe ("BNSF"). Skeptics of the transaction/remedy package complained both that the volume of trackage rights was inadequate and that the negotiated trackage (access) fees were too high to permit adequate competition between the BNSF and UP-SP. Department of Justice, *Press Release*, April 12, 1996 (www.usdoj.gov/opa/pr/1996/April96/163.at.htm); Department of Transportation, *Press Release*, June 3, 1996 (www.dot.gov/affairs/1996/dot13096.htm); Resolution of the Utah Legislature. In the end after a careful analysis of the likely direct competitive impact of the merger proposal, the Board approved the merger along with a remedy targeted at eliminating adverse competitive consequences arising specifically from the merger. The Board did not order unrelated "competitive enhancements" and has resisted doing so subsequently.

The UP-SP merger has *not* created "demonstrable competitive problems" and "the (Surface Transport) Board found no negative competitive effects stemming from the merger." As predicted by proponents of the merger at the time, the Board has concluded that "the UP-SP merger has produced vigorous competition and improved service in the West." Surface Transport Board, *Press Release*, December 15, 2000 (www.stb.dot.gov/newsrels.nsf/.../a8f0485edef04218852569b60055c946?OpenDocumen), and STB, *Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company—Control and Merger—Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and the Denver and Rio Grande Western Railroad Company*, Decision No. 16, December 13, 2000. With a record of sound merger decisions, the current policy that links remedies to any problem created by a merger should not be overturned.

articulate and address any anti-competitive concerns due to prospective merger-related increases in market power that could harm consumers.

III. Rail Competition for "Captive" Shippers

29. End-to-end, or vertical, mergers do not eliminate directly competing firms offering parallel point-to-point service. End-to-end mergers permit firms to offer single-line long-haul service, may result in service improvement (measured by car cycle time), and may result in a better assignment of railroad responsibility for delivery that is prompt and avoids damage-in-transit during long (or longer) hauls than arises when multiple railroads share the movement.[23] "End-to-end" mergers are unlikely to create additional "captive" shippers. In any event, the Board's conditioning powers should be sufficient to address any competitive issues arising in this context.

30. A truly "captive" shipper cannot use or credibly threaten to use any mode at a reasonable cost except its current rail carrier.[24] A plant directly served by just one railroad may have more competitive *rail* alternatives available to the owner than is readily apparent. Competition from other railroads may include (a) threats to truck to a nearby railroad, (b) threatening to build-out to

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23 For example, Don Phillips, "Alliance to Forge U.S.-Canada Rail System," *Washington Post*, December 21, 1999, A1, notes that "one of the dumbfounding long-term problems with railroading is that companies can't seem to hand off a rail car from one railroad to another without delaying it 24 hours or more." An editorial in the *Journal of Commerce*, September 28, 1999 observes that "poor coordination is still a major reason for poor customer service. ... Railroads have been trying to enhance computer links to improve inter-line management, but that process has been slow and is only now moving forward effectively." Prior to the Staggers Act, the best efforts of a financially healthy railroad to provide long-haul service could be thwarted if the connecting railroad's terminal and tracks were in poor shape and, so, delayed service or increase damage-in-transit. When two (or more) railroads share a movement, each railroad only considers the impact of its decisions to maintain or improve service *for that movement* on its own revenue, not on the revenue of the other participating railroads. The externality between railroads – one railroad's investment in service positively affects another railroad's earnings stream – can be internalized as a result of a merger. When externalities are positive – one party's actions benefit the other parties – economics teaches that too little of the externality-producing activity takes place: railroads invest too little in service quality.

24 Some railroad-shipper disputes arise when both the railroad and the shipper have dedicated assets (sunk costs) associated with their relationship. This is not a situation unique to the railroad industry. The same problem arises between a mine-owner and a coal-using utility the mine serves. In both cases, the mine and the utility may elect to negotiate a long-term contract before either party makes an irreversible investment decision, including an investment to expand or maintain either facility, and long-term contracts between mine-owners and electric utilities are widespread. Paul Joskow, "Price Adjustment in Long-Term Contracts: The Case of Coal," *J. of Law & Economics*, Vol. XXXI, April 1988: 47-83. Long-term contracts with volume guarantees permit a lower price to the utility that is also remunerative to the mine-owner. This occurs precisely because the volume guarantee reduces the risk of the investment in the mine. Moreover, prior to sinking the mine or building the railroad, both parties have other options. The mining company could elect to invest elsewhere if it concluded rail-rates would not permit the mine to earn at least a normal return over its lifetime, or the mining company might elect to connect to another railroad. Facilities as long-lived as mines are not the only ones where sunk costs are important. As time passes and new investment decisions are undertaken, even truly "captive" shippers obtain competitive alternatives. Recognizing this, over time shippers have been able to protect their interests by negotiating long-term contracts with railroads, often using the prospect of plant location or expansion decisions as leverage to obtain favorable terms.

another railroad, or (c) threats to shift production from the "captive" plant to non-captive plants or to "captive" plants served by another railroad.[25] Competitive alternatives that may also affect rates to "captive" shippers include competition from other geographic locations or competition from other products that a receiving shipper might use in lieu of the "captive" product.[26]

31. The volume of freight that is "captive" to railroads appears small.[27] Moreover, the Board's present policy addresses the concerns of shippers who would be made "captive" by a merger. The proposed change in general merger policy addresses *non-merger* issues that affect a small percentage of total freight traffic. The Board has not explained why it is necessary to change general merger policy – putting the Board in the process at odds with other merger-reviewing Agencies and its own prior precedent of not using merger review to address pre-existing conditions– to address non-merger issues that do not appear to be widespread.

32. Mergers that do not make additional shippers "captive"—either because the merger does not structurally do so, or because the merging parties agree to provide access to protect them—are inappropriate vehicles for the delivery of new regulatory measures intended to change the pre-merger condition of captive shippers. Shippers urging such new regulatory measures obviously see forced access as an alternative or additional negotiating lever to their existing maximum rate regulation rights. But, adopting the sort of forced access conditions that have been proposed in the context of merger proceedings would undermine the sound national rail rate regulatory policy as it has been formulated by Congress, implemented by the Board and its predecessor, and approved by the courts.

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25 The "threats" must be credible or *perceived* as credible by the incumbent railroad. Both the railroad and the shipper negotiate with some uncertainty about the other party's alternatives to reaching a deal. *Both* the railroad and the shipper lose from the ending of a relationship that would have provided the railroad with revenue above incremental cost and would have provided the shipper with service costing less than the next best alternative.

26 Prior to January 1999, the Board included both geographic and product competition in its analysis of mergers *and* rate reasonableness. This approach is entirely consistent with the practice of the other agencies charged with reviewing mergers and should be reinstated. Including product and geographic competition as factors for consideration certainly does not require a finding that either form of competition is a realistic alternative. For a given merger (or a given rate reasonableness determination), a receiving shipper, however, may economically use alternative products or the same product may be received from (shipped to) other geographic areas over either other railroads or by other modes. Excluding both factors from consideration leads to overestimates of market power. Neither type of potential competitive constraint is unique to transportation mergers or market power determinations.

27 According to Grimm & Winston, "Competition in the Deregulated Railroad Industry: Sources, Effects, and Policy Issues," in Sam Peltzman and Clifford Winston, eds., *Deregulation of Network Industries* (Brookings, 2000), 19.6 percent of rail freight is currently "captive." However, according to the Commodity Flow Survey, in 1997 railroads accounted for 4.6 percent of freight by value, 14.0 percent by tonnage, and 38.4 percent by ton-miles. Hence, "captive" freight accounts for 0.9 percent of shipments by value, 2.7 percent by tonnage, and 7.5 percent by ton-miles. The 1997 Commodity Flow Survey figures differ slightly from data used by, for example, the AAR. AAR cites slightly higher rail use rates—25 percent by tons and 40 percent by ton-miles—which raise the "captive" freight calculation slightly—to 4.9 percent by tons and 7.84 percent by ton-miles.

33. Furthermore, such new regulatory measures are inappropriate if they are seen as alternatives to a "rate-reasonableness" inquiry, and if they effective in inducing new entry that would otherwise not occur. This is so, as discussed below, because such new entry is likely to be inefficient. However, if the standard for a "competitive enhancement" access grant during a merger is the same as a "rate reasonableness" inquiry, then it is at best redundant, while still likely to foster inefficient logistical arrangements. The Board's SAC standard for its review of captive–shipper rates for "reasonableness" is founded on sound principles and has the potential to provide the optimal guidance and oversight for efficient pricing to end-users.

IV. Benefits Arising Following Deregulation and the Railroad Consolidations that Ensued

34. Dramatic productivity improvements in the nation's railroad operations followed the implementation of the Staggers Act, including improvements flowing from mergers, and proved to be of significant benefit to consumers.[28] These improvements are the true "competitive enhancements" the Board should encourage. With rate flexibility and the use of efficient (e.g. Ramsey) pricing principles, it is quite likely that some shippers have received larger rate reductions than others. Given substantial differences among shippers in both the incremental costs of their services and their elasticities of demand, it would be surprising indeed if real rate reductions *had* been uniform. However, I have not seen any careful analysis showing that "captive" shippers have failed to benefit by paying lower rates than they would have paid had the pre-Staggers regulatory environment continued.[29] *All* (or nearly all) rates have fallen even though the *current* rates paid by "captive" shippers exceed the rates paid by shippers with less willingness-to-pay for rail service, perhaps as a result of having attractive logistical alternatives.

V. Volumes of Freight Service: Rail, Truck, and Water by Major Categories

35. It is beyond serious debate that railroads since passage of the Staggers Act (1980) have become more efficient. The Staggers Act promoted far more efficient use of railroad assets by eliminating the regulatory burdens and misincentives that had been preventing rail network rationalization, realization of economies of route density, and realization of economies of scale and scope. Since 1980, pricing has become more efficient as it has been based upon both the cost and demand characteristics of service. Optimal price-setting when economies of scale and scope are significant[30] results in prices that raise a given amount of railroad revenue in the least painful

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28 Clifford Winston, et al., estimated that rate reductions conferred benefits directly on shippers (and indirectly through shipper competition on final consumers) worth $12 billion by 1989. Winston, et al, *The Economic Effects of Surface Freight Deregulation* (Brookings, 1990). The mergers that occurred during the 1990s have, evidently, not eroded these post-deregulation gains. The Board Study concludes that shippers paid $31.7 billion less in 1999 than they would have paid had revenues per ton-mile remained at inflation-adjusted 1984 levels.

29 This, of course, heroically presumes that railroads would have remained sufficiently solvent to continue providing acceptable service.

30 Optimal pricing in this context frequently goes under the rubric "Ramsey-Boiteux pricing." The classic modern reference is William Baumol and David Bradford, "Optimal Departures from Marginal Cost Pricing,"

way to consumers. Any other approach to pricing transportation services may well make *all* parties worse off. Because horizontal or "parallel" mergers have the potential to both enhance market power and result in efficiencies, the net result with respect to rates cannot be predicted in advance. If the wave of mergers that followed the Staggers Act had increased market power to the net detriment of consumers, one would expect to have seen higher, not lower, rail rates in real terms.[31]

36. Productivity increases in railroading following the Staggers Act have been impressive. According to Bureau of Labor Statistics data, multifactor productivity over the twelve year

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American Econ. Rev., June 1970. The basic principle linking efficient prices to both cost and demand was recognized 120 years earlier by the French engineer/economist Jules Dupuit, "Des peages," *Annales des Ponts et Chaussees: Memoires et Documents*, 2d ser., 17 (1): 207-248; translated by Elizabeth Henderson, *International Economic Papers*, no. 11: 7-31, and discussed at length by Robert B. Ekelund, Jr. & Robert F. Hebert, *Secret Origins of Modern Microeconomics: Dupuit and the Engineers* (University of Chicago, 1999), Chapter 8. Prices that varied by both cost and demand conditions became a staple of railroad rate-setting by the mid-late 19th century. Arthur T. Hadley, *Railroad Transportation: Its History and Its Laws* (G.P. Putnam & Sons, 1886).

The original purpose behind what has become known as Ramsey pricing was to find a price structure that raised a given amount of money above incremental cost—an amount at least sufficient to cover the common (shared) costs of e.g. a bridge, a canal, a railroad or a toll road—while reducing traffic by the smallest amount. Subsequently, Ramsey and Boiteux discovered that a regulator interested solely in maximizing the welfare of consumers, subject to the requirement that the supplier remain viable, would set prices in a way that looked remarkably similar to the differential pricing structure railroads, and railroad economists, discovered in the 19th century. The Ramsey-Boiteux price structure links the price charged to a customer's elasticity of demand, in the case of independent demands, or to a customer's "superelasticity" when demands are interrelated. When the sum of money to be raised just covers the total forward looking cost of serving all the customers using the shared facility (including a normal risk-adjusted return), the price structure is "Ramsey-optimal". In the real world of transportation and railroads, some rail services face significant competition (trucks, barges, relocation of plants, etc.), while others do not. For simplicity, suppose railroads face two customers, one with good alternative options and one without them. The railroad bears shared costs of $1,000 and incremental or variable costs of $200 for the "competitive" shipper and $300 for the "captive" shipper. In the market for transportation services, the railroad can charge the "competitive" shipper $250. So long as the "captive" shipper is charged no more than $1,250—the difference between total cost for serving both customers ($1,500) minus the revenue earned by serving the "competitive" shipper ($250)—prices satisfy the Ramsey test, provided the "competitive" shipper pays at least its incremental cost ($200). The railroad is allowed to compete for competitive traffic so long as its rates there cover incremental cost. Anything above incremental cost the railroad earns offsets shared costs and thus reduces the burden "captive" shippers would otherwise bear to have service provided to them. Finally, as in competitive markets, the maximum amount even a "captive" shipper pays is the stand-alone cost (SAC) of providing service. This is, in essence, the approach taken to rate-reasonableness under the Staggers Act, as implemented by the Board and the ICC. Railroads can earn as much from competitive traffic as possible—provided they recover incremental cost—and rates to captive shippers are capped by SAC .

31 Indeed, an argument can be made that policymakers, including Congress, *expected* at least some rail rates to rise following the Staggers Act because the pre-Staggers era of "rate equalization" and "open routing" had resulted in a very inefficient rate structure that was maladapted to properly recovering total cost of service. Hence, differential pricing was expected to result in higher rates to some shippers than they had previously paid, while allowing lower rates to be charged for other types of service e.g. facing more inter-modal competition. That an array of studies have indicated that rates for all types of rail traffic have fallen in real and nominal terms since 1980, 1984 and 1990 is therefore a remarkably telling indicator of the productivity gains accomplished as a result of regulatory reform and restructuring through mergers.

period, 1966-1978 increased on an index basis from 50.5 to 67.3, or 2.4 percent per year. In dramatic contrast, over the twelve years following the Staggers Act, 1981 to 1993, it increased from 67.7 to 129.0, or 5.5 percent per year. The BLS index of output per hour over the latter period rose nearly 200 percent, from an index value 55.1 to 145.6. During the earlier period, it rose from 33.8 to 51.6, or about 50 percent.

VI. Recent Studies of Rail Rates

37. Economic analysis of competition faced by railroads coupled with the efficiencies resulting from better operating techniques, more efficient labor utilization and better realization of network and density economies of scale and scope, strongly suggest that rail rates during the post-Staggers Act period – the period characterized by significant railroad consolidations – should have fallen. At the same time, the fraction of intercity traffic handled by railroads, as they became more efficient and passed efficiency gains through to consumers, should have increased at the expense of other modes.[32] The Staggers Act deregulation as implemented by the Board and its predecessor, the ICC, permitted economically rational – efficient – differential pricing and thus eliminated costly distortions –inefficient discrimination – in the rate structure designed to subsidize certain small shippers, certain ports, and certain producing areas.[33]

38. Recently studies released by the Board's Staff ("Board Staff Study") and the General Accounting Office ("GAO Report") strongly support these predictions.[34] The GAO Report and the Board Staff Study do not provide any support for changes in the Board's policy toward merger remedies. The Board Staff Study makes the following points:

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32 This occurs when rail productivity-improvement exceeds the improvement in productivity from competing modes of transportation. If both rail and truck productivity had increased at about the same rate following transportation deregulation, then intermodal competition would have resulted in lower rates, but need not significantly have shifted total intercity traffic share from one mode to the other.

33 Kenneth Boyer, "Equalizing Discrimination and Cartel Pricing in Transport Rate Regulation," *J. of Political Economy*, Vol. 89 (April 1981): 270-286, describes the inefficiencies and cross-subsidies arising out of pre-Staggers Act regulation.

34 These studies confirm predictions made in the 1980s regarding the likely results of deregulated rates and the strength of the competitive-constraints railroads faced. Theodore E. Keeler, *Railroads, Freight, and Public Policy*, (Brookings, 1983); Michael Babcock, "Potential Impact of Railroad Deregulation in the Kansas Wheat Market," *Journal of Economics*, Vol. 7 (1981): 93-98; Stephen Fuller, et al., "Effect of Railroad Deregulation on Export Grain Rates," *North Central Journal of Agricultural Economics*, Vol. 5, No. 1 (January 1983): 51-64; J.C. Shouse & M.A. Johnson, *Anticipated Consequences of Seasonal Railroad Rates in the Oklahoma Wheat Transportation Market*, Oklahoma State University Agricultural Experiment Station, Research Report P-773, 1978; William W. Wilson, et al, *Impacts of Seasonal Rail Rates on Grain Flows and Storage in North Dakota*, Upper Great Plains Transportation Institute, North Dakota State University, Report 37, March 1981; U.S. Department of Agriculture, Office of Transportation, *An Assessment of Impacts on Agriculture of the Staggers Rail Act and Motor Carrier Act of 1980* (GPO, August 1982); Richard C. Levin, "Railroad Rates, Profitability, and Welfare Under Deregulation," *Bell J. of Economics*, Vol. 12 (Spring 1981): 1-26; Michael Babcock & H. Wade German, "1985 Forecast: Rail Share of Intercity Manufactures Freight Markets," *Proceedings of the Transportation Research Forum—1983*, Vol. 24, No. 1; James M. MacDonald, "Railroad Deregulation, Innovation, and Competition: Effects of the Staggers Act on Grain Transportation," *J. of Law & Economics*, Vol. XXXII, April 1989: 63-96.

- "After adjusting for inflation, railroad rates fell 2.7 percent in 1999, with rates in the East declining 2.6 percent and rates in the West falling 2.8 percent. … (I)nflation-adjusted U.S. rail rates have fallen 45.3 percent since 1984.
- "Rates have fallen even *before* adjusting for inflation. (S)ince 1984, and with no adjustment for inflation, eastern rail rates have fallen 13.2 percent, western rail rates have fallen 24.7 percent, and rates for the nation as a whole have fallen 19.7 percent.
- "When the Staggers Rail Act of 1980 (Staggers Act) sharply curtailed the rail regulatory powers of the Interstate Commerce Commission, most knowledgeable observers believed that railroads would use their new-found pricing freedoms to raise rates. Instead, numerous academic studies have confirmed that rail economic regulatory reform resulted in significant economic efficiency benefits, most notably rapid productivity growth, that enabled railroads to become financially stronger while lowering average rate levels. This rate study suggests that, while there are clearly instances where railroads retain a degree of pricing power, nearly all of the productivity gains have been passed along to rail customers (and ultimately consumers) in the form of lower rates – evidence that, on the whole, the railroad industry clearly operates in a competitive environment.
- "It is important to note that all types of rail customers, and not just those with competitive transportation alternatives, must have received some portion of the rate reductions we have measured here. Otherwise, there would be evidence that all shippers limited to rail as a transportation option and served by a single carrier would be paying rates that were, on average, well over twice the amount charged to shippers of the same commodity who receive more competitive rail service. … There has not been a claim that rates systematically vary to such a significant degree. To the contrary, there is no firm evidence that the rate gap between exclusively-served and other rail shippers has widened appreciably since 1984.
- "While some portion of the decline in rail rates that we have measured results from costs that have been shifted away from railroads and onto shippers, this portion is dwarfed by the most important factor responsible for the rail rate reductions – the productivity gains achieved by railroads since the Staggers Act. Comparing 1998 to 1980, Class I railroads produced 50 percent more ton-miles using 61 percent fewer employees, 28 percent fewer locomotives, 38 percent fewer track miles, and 23 percent fewer freight cars in service. It is this improvement in productivity that has driven the decline in rail rates, and a more efficient rail network is a clear benefit to the public at large."

The Board's approach, common with all other merger reviewing agencies, of (a) confining merger-remedies to competitive problems directly related to the merger itself and (b) making the remedies "structural" rather than "regulatory" has not resulted in approved mergers leading to higher rates to shippers or their customers.[35]

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[35] Earlier studies of the impact of rail mergers and deregulation on productivity and rates concluded that mergers have resulted in cost reductions and service improvements, although the effects on both have been small. Ernest Berndt, et al., "Mergers, Deregulation, and Cost Savings in the U.S. Rail Industry," *Journal of Productivity Analysis*, Vol. 4, 1993: 127-144; Alison Chaplin and Stephen Schmidt, "Do Mergers Improve Efficiency? Evidence from Deregulated Rail Freight," *Journal of Transport Economics and Policy*, Vol. 33, May 1999: 147-162. Recently, the Board's Staff has noted that the Union Pacific-Southern Pacific merger resulted in both more vigorous competition and improved service in the west.

39. The Board's Staff concludes that shippers in the aggregate would have paid $31.7 billion more than they actually did in 1999 had revenue per ton mile remained at its inflation adjusted 1984 level.[36] But where did the money go? Shippers may claim the alleged lower rates have not helped *them*. There is no reason to believe that lower transportation rates were *intended* to do so, however. In a competitive economy, as the Board Staff points out, reductions in the price of intermediate goods and services are not *expected* to remain with shippers or producers of final goods and services. Competition among shippers results in these savings being passed through to final consumers. What may motivate shippers most in a highly competitive marketplace is the fear that somewhere, someone is getting a better deal for transportation (or labor, or raw materials, or equipment).[37] Concerns about the cost of specific inputs, including transportation services, may be strongest where shippers face more, rather than less, competition from firms that do not depend upon the same input supplier(s).[38] However, when a railroad's customers face strong product-market competition from rivals that do not depend upon it for transportation service, higher rail rates cannot be easily "passed through" to final customers. A railroad raising rates above competitive levels risks undermining the viability of its own customers and sooner or later losing their business.

VI. Service Quality and Competition

40. While the Board's recently released review of the UP-SP merger indicates that service in the West improved, careful economic merger analysis considers whether and when a merger may

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36 Moreover, the Board Staff Study rejects the contention that the rate-savings has been illusory because railroads shifted costs to shippers (e.g., car ownership). The Staff estimates that the total annual cost of shifted car-ownership would be no more than $2.5 billion, a number simply swamped by the estimated $31.7 billion shipper savings. The Board Staff Study also describes as "small" the measured rail-cost reductions arising from switching from single-car to multi-car or unit-train operations. Moreover, the switch to more efficient shipping arrangements may have itself been due to greater flexibility given railroads as part of the Staggers Act. Hence, the bulk of the reduction in shipping costs between 1990 and 1999 cannot be attributed either to cost-shifting or to changes in the mix of rail transport services.

37 If railroad mergers and deregulation have resulted in better rail service – faster delivery and less damage-in-transit – as well as lower rates, it is entirely possible that shippers – whether at the origin or destination – face more intense competition. A recent antitrust analysis of the market for western coal concludes that the DOJ's 1982 geographic market "cannot stand in light of subsequent developments…the DOJ's geographic markets should be broadened for several reasons," including the fact that "[t]ransportation costs for most coal producers have fallen significantly since 1983, primarily as a result of new railroad investment … and new rail competition serving the key, coal-producing regions." Mark A. Glick, David G. Mangum, and Raymond J. Etcheverry, "Mergers in Western Coal Markets: Conforming Antitrust Analysis to the New Reality," *West Va. Law Review*, 1997 (Available on the Internet at www.econ.utah.edu/les/mergers.html). Falling (rising) transportation rates, much like falling (rising) tariffs, can widen (narrow) relevant markets and by doing so change the degree of competition that transport service-using firms face.

38 This sort of concern apparently motivated the ICC's "freight equalization" doctrine. It was held that all shippers of a given commodity within a region should pay the same freight rate regardless of differences in cost of service. The resulting potential for inefficiency is plain from the perspective of current-day economics.

result in reduced service quality rather than or in addition to higher rates. It is important to understand that service-quality *deterioration* is *not* inherently profitable for a firm with market power.[39] For example, when the impact of a change in quality on profits is independent of the quantity of service being provided, then a monopolist will provide the same quality level as a competitive industry does.[40]

41. It is most important to emphasize that the principal efficiencies that result from beneficial mergers are often associated with higher quality products and services, as well as with higher productivity gains and lower production costs. The increased levels of investment in infrastructure, rolling stock, and control systems that beneficial mergers motivate and enable can be expected to contribute greater reliability of service, greater capacity to provide service, and better attributes, like speed and smoothness, of service, even as they lower the need to expend other categories of costs. The evidence is consistent with this view of the impacts of most of the railroad mergers since the implementation of the Staggers Act by the I.C.C. and the Board. Of course, there have been some service integration difficulties in these mergers. These have proven to be transitory-- a difficult and painful transitional episode that indicates neither market power nor the absence of longer-term efficiencies from the combination.

VIII. Forced Access Creates Inefficiencies and Unintended Costs

42. Railroads are network firms, and as such they are highly sensitive to network-related economies of density, scope and scale. Networks typically require significant coordination across the network's segments precisely because activity on one part of the network can impact operations elsewhere. Moreover, rail networks are highly capital intensive with substantial sunk,

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39 To the contrary, reduced service quality brought about by, for example, increased car dwell in terminals adds car cost and increases yard congestion. This makes operations within the yard less fluid and more expensive. Trains stranded on line of road when their crews reach their hours of service limitations add additional crew starts and also increase costs. Locomotive availability becomes a problem and the carrier must seek out more units— again at substantial additional cost. As lower quality may paradoxically *increase* costs, it also can reduce revenue. For just as customers are sensitive to rail rates, they are also sensitive to service quality and can, or do, shift to other transportation modes from whom the railroads may be hard-pressed to win them back.

40 The literature on how market structure affects quality is a long one. For a review, see John Beath & Yannis Katsoulacos, *The economic theory of product differentiation*, (Cambridge University Press, 1991): Chapter 5.

To my knowledge, there has been no careful empirical study that supports the claim that service quality (e.g., cycle time) is either lower or has been reduced where rail-to-rail competition is absent. Curtis Grimm & Clifford Winston, op cit. measured service quality by cycle time and concluded (p. 65):

> We investigated whether captive shippers receive worse service than noncaptive shippers by replacing the competition variables in the average and standard deviation of service time models with the captive shipper dummy. In contrast to our finding for freight charges, the parameter estimate for the dummy is statistically insignificant in both models, which indicates that captive traffic does not experience greater unreliability or take longer to get to its destination than noncaptive traffic.

joint and common costs. The shared assets giving rise to these common costs provide services supporting many types of traffic, including unit train movements of coal, grain and other bulk commodities, single car general merchandise movements, and intermodal trains. The assets and their cost are not explicitly attributable to any specific car or train movement. When traffic is not being subsidized, each type of traffic will make some, albeit possibly small, contribution to the recovery of the common, fixed and sunk costs that is necessary for railroads to be commercially viable.

43. Economies of density are realized when any given part of the network carries increased volume at a lower average cost. As the route density of traffic handled by a single carrier increases, the average cost of service tends to decline for all involved shippers.[41] Lower average cost per unit carried arise not only from greater spreading of fixed costs over a larger traffic base, but also from efficiencies in operations as train size increases. As density grows, freight car, locomotive and crew utilization become more efficient. Increased train frequency with concomitant service enhancement may also become practical as volume thresholds are reached.

44. To accommodate a multiplicity of movements with each taking a specific car from its origin to its destination, the carrier must balance priorities. Yard capacity limitations must be traded off against blocking needs and opportunities. Train start decisions require balancing of costs, locomotive and crew availability and line capacity. Priority decisions among trains constantly present tradeoffs. In the end, the efficient use of a specific line segment or terminal, or the costs of providing specific service levels to given shippers, cannot be determined independently of the efficient use of the rail network. Making efficient use of the network requires substantial and significant coordination across routes, terminals, and customer shipments.

45. Compulsory access—introducing a new entrant whose use of rail assets is intrinsically no more efficient than that of the incumbent—injects a complex new factor into the calculus and is very likely to reduce rail efficiency and increase total costs. Dividing traffic between the incumbent and the entrant may well undercut economies of density and create costly coordination issues. In short, any forced access will likely have some impact on the incumbent owner's economies of density, scope and scale. This will potentially increase the incumbent's per-unit costs, interfere with operational efficiency, and thereby tend to degrade service to all affected customers and raise the per-unit costs of providing service to shippers throughout the network. The more extensive the forced access, the more extensive these undesirable effects will potentially be.

46. The current NPR grafts onto objective merger analysis an entirely subjective component – unrelated "competitive enhancements" – that appear to constitute an invitation and prescription for parties unaffected by a merger to reach, under the authority of the Board, into the (potentially) deep pockets of the merging parties. Any remedy to a perceived competitive problem arising

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41 Economies of density along a single line can be realized so long as the complementary yard and terminal assets associated with such movements are not congested. They are also limited by the basic physics of railroad track and roadbed and the organizational ability of railroads to safely schedule more and more movements.

from a merger ought to be targeted in the relevant market to bolster the competition that would benefit the customers who would otherwise be injured. There is nothing in economics supporting the notion that robbing Peter to pay Paul is fair or equitable, much less efficient. Yet that is precisely what a policy of unrelated "competitive enhancements" does. Such an approach would put the Board squarely at odds with the merger policy programs of other federal agencies with merger review authority, and on the wrong side of the discrepancy from the viewpoint of the public interest.

47. Leading candidates for the "competitive enhancements" seem to be forced access arrangements. Because these arrangements would be forced, and yet unrelated to particular competitive concerns from the merger, they almost surely would be contributors to inefficiency rather than helpmates to genuine competition. As discussed above, there is a great deal at stake in terms of network costs, loss of network economies, and degradations of other shippers' quality of service, and economic logic indicates that such forced access arrangements are likely to cause serious problems of inefficiency.

48. It is particularly important to recognize the mistakes that this course would entail in railroading today for several reasons. First, as discussed at length above, and as the Board well knows, the dramatic successes of the U.S. rail industry since the implementation of the Staggers Act by the I.C.C. and the Board were caused by deliberate disavowal of this very kind of distorting regulatory intervention. It cannot be emphasized enough that requiring competitive enhancements would be an extremely dangerous return to the worst errors of pre-Staggers railroad regulation.

49. Second, railroads, unlike telecommunications or electric utilities, have been subject to foreclosure-defeating access requirements for quite some time. As common carriers, railroads must provide rates and routes to move traffic tendered by a shipper from any origin to any destination and must interchange with other railroads if necessary to complete the movement.[42] Railroad also cannot foreclose interlined routes that are more efficient than their own single-line routes by either refusing to deal with other railroads or demanding an excessive share of joint revenue.[43] However, railroads are *not* required to enter into any joint route a shipper may suggest, regardless of its efficiency.[44] Yet, the Board can order temporary access to remedy service emergencies. In addition, the Board retains the right to review rates, including single-line rates, for reasonableness under its usual rational standards. (The Board can analyze rates set

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42 49 U.S.C. ¶ 11101; Ex Parte No. 528, *Disclosure, Publication, & Notice of Change of Rates & Other Service Terms for Rail Common Carriage*, Decision served May 3, 1996, p. 4, n. 4. 49 U.S.C. ¶¶ 10703, 10742; *Routing Restrictions Over Seatrain Lines, Inc.*, 296 I.C.C. 767, 773-774 (1955).

43 Under traditional joint rate-making principles, all carriers participating in a joint rate had to agree to rate changes. When railroads participate in "multiple independent factor through rates" ("MIFTRs") participating carriers can unilaterally increase or decrease their part of the joint rate. Docket No. 40298, *Society of the Plastics Industry, Inc. v. Consolidated Rail Corp.*, Decision served Oct. 22, 1990, *aff'd sub nom. Society of the Plastics Industry, Inc. v. ICC*, 955 F.2d 722 (D.C. Cir. 1992).

44 49 U.S.C. ¶ 1144.5; *Vista Chemical Co. v. Atchison, Topeka & Santa Fe Ry.*, 5 I.C.C. 2d 331, 341-342 (1988).

above 180 percent of variable cost for "reasonableness," and rates can be compared to the stand-alone cost of providing service.)

50. Third, shippers that may perceive themselves to be "captive" to a bottleneck segment may actually have means by which they can apply real competitive pressures to their carriers in order to obtain attractive rates and service. For example, such a shipper could 1) threaten to build-out to a nearby carrier, 2) threaten transloading from rail carrier to truck, 3) shift portions of the "captive" facility's output to other "non-captive" plants, 4) use the leverage of a new plant or capacity expansion decision to protect its interests at the "captive" location, and the list goes on.[45]

51. In contrast to the harms from forced access, the efficiencies flowing from a merger *are* genuine "competitive enhancements," and they are precisely the competitive enhancements the Board should be concerned about. Aside from mergers, railroads can and have entered into voluntary contractual access-granting arrangements when it is efficient to do so.[46] These

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45 Even in cases where "essential facilities" were found to exist, they may prove upon more thorough examination to have been mis-identified because shippers or railroads had more options than was appreciated at the time. The antitrust case that established the "essential facilities" doctrine—*Terminal Railroad*—involved eight railroads that formed a joint venture to establish and operate terminals facilities in St. Louis, Missouri. A ninth railroad subsequently sought to enter the market and requested access, which the joint venture denied. The railroad denied access brought suit against the joint venture acting as a single entity. In effect, the plaintiff alleged that the St. Louis terminal and railroad bridges were a bottleneck access to which was "essential" for it to compete for trans-Mississippi freight. However, whether the terminal facilities in St. Louis proper was truly "essential"—impossible to avoid and economically inefficient to replicate—is not obvious. Andrew Kleit and David Reiffen, "Terminal Railroad Revisited: Foreclosure of an Essential Facility or Simple Horizontal Monopoly?," *J. of Law and Economics*, Vol. XXXIII, October, 1990: 419-438.

46 Access includes (a) terminal rights, including rights to limited amounts of mainline track, (b) trackage rights, (c) reciprocal switching rights and (d) the development of joint rates. The Cumberland Southern Railway offers an example (selected solely because it was publicly available) of apparently voluntary trackage rights granted prior to the Staggers Act. Cumberland Southern Railway, Clarksville Subdivision Train Digest and Procedure Manual, September 12, 1959, rev'd November 6, 1962. Cumberland Southern had granted trackage rights to the New York Central, the Pennsylvania, the Southern, the Seaboard, the Cincinnati & Toledo, and the New River Electric railroads, as well as to Calvin Coal Company and the Clinch Lumber Company. http://members.tripod.com/~cumberlandsouthern/csryoper.htm, accessed December 15, 2000. The Rock Island Railroad exited due to financial problems in the1980s, but the Rock Island was involved in trackage rights agreements with other railroads in Arkansas, Colorado, Illinois, Iowa, Kansas, Louisiana, Minnesota, Missouri, Nebraska, Oklahoma, Tennessee, and Texas. Railroads with whom the Rock Island had trackage rights agreements included the St. Louis & San Francisco, the Union Pacific, the Denver, Rio Grande & Western, the Denver & Intermountain, the New York Central, the Penn Central, the Milwaukee & St. Louis, the Chicago & NorthWestern, the Burlington Northern, the Missouri Pacific, and the Aitchison, Topeka & Santa Fe among others. Rock Island Trackage Rights, April 12, 1988, www.simpson.edu/~RITS/structures/ritrrts.html More recently, the Norfolk Southern received overhead trackage rights from the Bessemer & Lake Erie (a Class 2 railroad) over 50.4 miles of the B&LE's mainline between Shenango, PA (milepost G4.27 in Mercer County) and Wallace Junction, PA (mile post F8.90 in Erie County). The NS has indicated that the agreement permits the NS to "move traffic more safely, efficiently and expeditiously" in western Pennsylvania. Department of Transportation, STB, FR-4915-00-P, Norfolk Southern Railway Company-Trackage Rights Exemption-Bessemer and Lake Erie Railroad Company, www.railnews.com/NFS/ 001004NSFABN.htm. Another recent example of reciprocal access involves Driscoll Rail and the Canadian National exchanging trackage rights providing access to Boston and Long Island by DR in

arrangements also benefit shippers. Railroads most efficiently haul freight in large volumes (e.g., unit trains or multi-car shipments) under single-line movements. When doing so requires access rights, for example, railroads have an incentive to provide them to one another when and where it is efficient to do so. When it is *not* efficient to do so, compulsory access grants can undermine efficient long-haul single-line movements by reducing route density or by permitting a higher cost carrier—higher costs "above the track"—to carry the freight, when it could not under genuinely competitive conditions.

52. Compelled access – "competitive enhancement" – is likely to be economically and socially inefficient for several reasons. First, compelled access will invariably be inefficient because it will occur only when the railroad receiving access rights is less efficient that the incumbent.

53. Suppose Railroad 1 provides through service to a shipper desiring such service from Philadelphia to Detroit via Toledo. Railroad 1 provides bottleneck service from Toledo to Detroit. The incremental cost, IC(PD), of this movement is composed of all "costs above the rails" from Philadelphia to Toledo, IC(PT), and from Toledo to Detroit, IC(TD), plus "wear and tear" on the track. The rate, R, is presumably reasonable, as it is either less than 180 percent of incremental cost or no higher than the stand-alone cost ("SAC") of the movement the shipper seeks. Suppose an alternative railroad could provide service from Philadelphia to Toledo at a lower cost than Railroad 1 – including all cost associated with negotiating a and maintaining a joint-rate[47] and any interchange required. Then Railroad 1 could provide access to its bottleneck

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return for access to CN terminals in Detroit and Chicago. Driscoll Rail Corporation, press release, 1997. www.tufts.edu/~rdriscol/driscoll-rail/News1997/news12nov97.html The Burlington Northern's Wisconsin Subdivision granted Norfolk Southern trackage rights on all BN main line track connecting LaCrosse and Portage, Wisconsin in 1998. The access gives NS a gateway to the Mississippi River and to Minneapolis, MN. Burlington Northern, press release, http://wisconsinsub.railfan.net/ns.html, accessed December 15, 2000.

As the Board notes in its 1996/1997 *Annual Report*:

> Trackage rights arrangements allow one carrier to perform local, overhead, or bridge operations over the tracks of another carrier that may or may not continue to provide service over the same line. ... The Board maintains a class exemption, at 49 CFR 1180.2(d)(7), providing a simple notification procedure for the acquisition or renewal of trackage rights by carriers *through mutual agreement that are not in response to a rail consolidation proposal.* All of the *159* trackage rights arrangements authorized by the Board in FY 1997 were processed under the class exemption.

This certainly suggests that "mutually agreed" forms of inter-railroad access occur voluntarily and are not solely the result of "fixes" to proposed mergers.

47 Joint rates create incentive problems that may result in inferior service. First, simply coordinating service across railroads may be more difficult than doing so internally. Second, each railroad is responsible for only part of the movement. If one participating railroad reduces service quality to lower its own costs – given the division of the joint-rate it will receive – some of the consequences of "cutting corners" will be borne by the other participating railroads. The shipper knows only that service has deteriorated. It does not know whether one or all of the railroads involved in the joint-rate are responsible. If, given the service deterioration, the shipper has an alternative, then the cost of poorer service will be borne by all the railroads, not solely by the railroad at fault. When one railroad receives the benefits of reducing service quality, while the potential costs of "cutting corners" are shared, each railroad has a greater incentive to shade quality than is true for a single-line movement.

Toledo-Detroit route and be no worse off than when it provided single-line service. Indeed, Railroad 1 could provide a joint-rate with a division that simultaneously makes all parties better off. However, if the entrant is less efficient, then entry that provides a lower total rate to the shipper must result in a rate for the Philadelphia-Detroit movement that is less than SAC(PD).[48] For the Board to avoid inefficient access would immerse it in long and costly hearings, while ignoring the efficiency of the access being sought would risk recreating the pre-Staggers Act problems associated with "rate equalization" and "open routing."

54. Second, investments in new services, facilities, or routing options are inherently risky. When these investments involve sunk costs it is well-recognized that if a shipper cannot credibly commit to refrain from switching to an alternative supplier then either rates will be higher or the service will not be provided.[49] Rules that allow the Board to compel access undermine the credibility of shipper commitments to deal exclusively with railroads providing new facilities, and this can keep service from even being available.

55. Consider the following simple ABC linear railroad network. Suppose only one railroad links AB, while several railroads, including the "bottleneck" railroad, serve BC. The AB "bottleneck" railroad provides single-line service from A to C. The AC rate equals the stand-alone cost ("SAC") of the AC line ("SAC(AC)"). A contract rate covering SAC(AC) may be a single-part or a multipart tariff.[50] Suppose the bottleneck railroad were required to quote a rate

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48 Suppose SAC(PD) = $1000, while IC(PT) = $400 and IC(TD) = $200. This implies that the full forward looking fixed (shared) cost of the movement is $400. Suppose a second railroad has incremental costs of $500 and quotes the shipper a $500 rate on the PC portion of the route. If the Board required Railroad 1 to quote a "bottleneck" route that would be subject to challenge, Railroad 1 would be limited to a rate of $360 for the TD portion of the move ($360 is 180% of $200, Railroad 1's incremental TD cost). The total out-of-pocket cost of the move rises from $600 to $700 and the total rate falls from $1000 to $860, or $140 less than SAC(PD). In a competitive market, efficient prices lie between incremental cost and the stand-alone cost of providing service. If a railroad earns less than incremental cost for a movement, the shipper receiving that service has gotten an economic (as opposed to an accounting) subsidy. Presuming that demand for service is certain, a shipper charged more than the stand-alone cost of service (including a normal return on investment) would, in a competitive market, either supply the service internally or find an alternative supplier.

49 Suppose a railroad makes an irrecoverable ("sunk") $1,000 investment in new facilities serving a shipper. The economic life of the facility is 5 years. Ignoring discounting, if the shipper agrees to use the facility for five years, the railroad can charge $200 per year for use of the facility and recover its investment. However, if the shipper does not or cannot make this commitment, the railroad will charge more – possibly as much as $1,000 in the first year, effectively selling the facility to the shipper. When customers cannot commit to long-term agreements one result is that the shipper, rather than the railroad, may be obliged to build new facilities. However, when facilities provide services that are shared by several shippers it becomes more difficult to efficiently arrange for joint supply. Moreover, when railroads – common carriers – build facilities they have an obligation to provide access to these facilities to the public. When shippers build the facilities – either individually or collectively – they do not have an obligation to make those facilities available to others – including new competitors.

50 A common example of a multiple-part tariff is a volume discount schedule – the rate declines as successively larger volumes are purchased. The simplest example is a two-part tariff used e.g. by utilities. The tariff consists of a fixed fee (a "hook-up" charge), F, that does not depend upon volume and gives the buyer the right to purchase unlimited quantities as a fixed price, r. The total amount the buyer pays for buying Q units of service is $C = F + rQ$. The average rate, $F/Q + r$, declines with volume purchased. The marginal price – the price paid for the last unit –

over the AB segment separately and accept any traffic offered originating at C. One immediate consequence could well be higher costs over the BC segment if the requirement to interline with all BC carriers divided traffic and reduced density on the bottleneck railroad's line. More important, a rival railroad with track connecting BC would be willing to carry traffic on the BC portion of the move so long as the rate covered incremental cost ("IC(BC)"). By forcing the AB railroad to interchange, switch, or haul for the "entrant," the revenue earned on the AC move would fall below SAC, assuming as I have that it began there.[51] Rates may not, however, exceed SAC regardless of Board oversight. As the GAO recently noted, railroad return on investment between 1990 and 1997 was less than the railroads' cost-of-capital in each year.[52]

56. Last, some forced access may frustrate competition rather than promote it. Access, as the I.C.C. and the Board have recognized, cannot be divorced from the *price* charged for access, and that fact will, if the current NPR proposals are adopted, ultimately inject the Board back into extensive rate-regulation. As an example, the Florida East Coast Railway Company ("FEC") sued CSX claiming that CSX had an obligation to provide FEC with a form of "most favored nations" treatment with respect to rates and routes, including confidential contract rates CSX negotiated with shippers following passage of the Staggers Act.[53] It is widely accepted by economists that contemporaneous "most-favored nations" agreements can possibly reduce or eliminate competition. When CSX successfully competed for General Motors business via its single-line

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is the constant, r. If r is set equal to marginal cost, then any buyer who elects to participate by paying F pays marginal cost for each incremental unit. It is the fixed fee that enables the seller to recovers all or some of the costs common to producing all units of output, and any profit. . This form of pricing, which is relatively common, mitigates or eliminates the output-reducing effects associated with market power and simple uniform pricing. Robert Wilson, *Nonlinear Pricing* (Oxford University Press, 1993). Hence, a bottleneck railroad may, even if it serves a single customer, price efficiently.

51 For a simple railroad, cost consists of (a) shared or common sunk costs and (b) incremental costs ("costs above the rails" plus wear and tear on the tracks). The Board can review rates that exceed SAC for a given movement. Current railroad access rules are based upon "efficient component pricing rules" ("ECPR"). For example, railroads cannot deny or terminate joint rates when the interlined route is more efficient than a bottleneck carrier's own single-line route. ECPR is necessary for efficient access to a bottleneck. ECPR does not address market power. However, the Board's rate review rules based upon 180% of variable cost and SAC *do*. Requiring access when the entrant is *not* demonstrably more efficient than the bottleneck carrier (or its joint-rate partners) results in inefficient entry that is very likely inefficiently to confine returns below revenue adequacy.

52 Between 1990-1997, the unweighted average annual return on investment was 4.72 percent *below* the cost of capital. While return on investment can be difficult to measure properly for industries like railroads, the point remains that there is no evidence that U.S. railroads earn supra-competitive profits.

53 *Florida East Coast Ry. Co. v. CSX Transp., Inc.*, Nos. 93-2601 & 93-2742, 7th Circuit, December 21, 1994 (www.kentlaw.edu/7circuit/1994/93-2601.html). CSX inherited an ICC-approved agreement arising out of the 1963 merger between Seaboard Air Line Railroad ("SAL") and Atlantic Coast Line Railroad ("ACL"). Prior to the merger, SAL provided single-line service into southern Florida and ACL and FEC provided competitive joint-line service. FEC protested the merger and, as the Court noted, "consistent with the then-favored policy of rate equalization, the Interstate Commerce Commission imposed...the requirement that SCL maintain through routes with FEC to southern Florida and establish joint rates for those routes that would be no higher than SCL's single-line rates. Such rate equalization *was possible because ICC approval exempted the merger from operation of the antitrust laws.*"

rate, FEC went to court to demand that CSX alter its joint-rates with FEC so that they would be equivalent to the single-line rate.[54] In effect, FEC sought to require CSX to provide (a) access via joint rates *and* to price that access so that FEC could participate in traffic moving into southern Florida regardless of whether joint-line service cost more than single-line service. This was one consequence of "rate equalization," and it is obviously anticompetitive and inefficient.

57. Proposals to provide so-called "competitive enhancements" are misnamed. They are, instead, anticompetitive. The Board's present policy focuses on the appropriate issue, namely identifying realistic instances of merger-related market power and providing a genuine procompetitive remedy.

IX. Conclusion

58. Making merger analysis presumption-free is a desirable goal. Presently that means eliminating the decades-old presumption, inherited by the Board from the ICC, that mergers are presumptively "good." Even had that been a justifiable rationale when railroads had too many miles of underused track and other assets, it is no longer so in the post-Staggers Act era. While presuming all mergers are "good" is not sound policy, it would be even worse to lurch to the opposite extreme by presuming all future rail mergers are inherently "bad". The best policy course is simply to analyze and judge each merger on its own merits.

59. The post-Staggers Act period, a period with many mergers, has not resulted in higher rates and worse service. Moreover, many economists predicted that deregulation—including unregulated markets for asset transfers—would result in better performance, better productivity, and more rational pricing. The evidence dramatically supports these predictions.

60. This does not mean that any and all proposed mergers have been free from competitive concerns. Rather, the Board's policy of analyzing each merger, identifying plausible competitive concerns, and then tailoring remedies to address these concerns has been quite effective, as the Board's recent review of the UP-SP merger illustrates. There is no general *merger-related* problem that requires a change in the way the Board handles this form of asset transaction aside from the major policy change of eliminating the decades-old presumption that mergers are invariably beneficial.

61. Proposals to require merging firms to do more than address competitive concerns arising directly from the merger are likely to be counterproductive and they are *not* "enhancements to competition." Instead they represent a dangerous return to the pre-Staggers Act forms of arbitrary regulation that nearly drove the industry into oblivion.

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[54] The Seventh Circuit ultimately held that the pre-Staggers Act FEC/SCL (CSX) agreement did not include contract rates and, so, it did not address the underlying antitrust issues that CSX had raised.

EXHIBIT RDW1 December 2000

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Professor of Economics and Public Affairs, Princeton University, 1978-.

Principal External Advisor, Infrastructure Program, Inter-American Development Bank, 6/97-8/98.

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Visiting Lecturer (with rank of Associate Professor), Department of Economics and Woodrow Wilson School, Princeton University, 1977-78 (part time).

Economics Research Department, Bell Laboratories, 1973-77.

Lecturer, Economics Department, Stanford University, 1971-73.

Other Professional Activities:

Advisory Board, Electronic Journal of Industrial Organization and Regulation Abstracts, 1996-.

Visiting Faculty Member (occasional), International Program on Privatization and Regulatory Reform, Harvard Institute for International Development, 1996-2000.

Member, National Research Council Highway Cost Allocation Study Review Committee, 1995-98.

Member, Defense Science Board Task Force on the Antitrust Aspects of Defense Industry Consolidation, 1993-94.

Editorial Board, Utilities Policy, 1990-

Leif Johanson Lecturer, University of Oslo, November 1988.

Member, New Jersey Governor's Task Force on Market-Based Pricing of Electricity, 1987-89.

Co-editor, Handbook of Industrial Organization, 1984-89.

Associate Editor, Journal of Industrial Economics, 1984-89.

Director, Consultants in Industry Economics, Inc., 1983-89, 1991-94.

Fellow, Econometric Society, 1981-.

Organizing Committee, Carnegie-Mellon-N.S.F. Conference on Regulation, 1985.

Board of Editors, American Economic Review, 1980-83.

Nominating Committee, American Economic Association, 1980-1981.

Research Advisory Committee, American Enterprise Institute, 1980-1986.

Editorial Board, M.I.T. Press Series on Government Regulation of Economic Activity, 1979-93.

Program Committee, 1980 World Congress of the Econometric Society.

Program Committee, Econometric Society, 1979, 1981, 1985.

Organizer, American Economic Association Meetings: 1980, 1982.

American Bar Association Section 7 Clayton Act Committee, 1981.

Principal Investigator, NSF grant SOC79-0327, 1979-80; NSF grant 285-6041, 1980-82; NSF grant SES-8038866, 1983-84, 1985-86.

Aspen Task Force on the Future of the Postal Service, 1978-80.

Organizing Committee of Sixth Annual Telecommunications Policy Research Conference, 1977-78.

Visiting Fellow, University of Warwick, July 1977.

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Consulting: Bell Laboratories, 1978-79; AT&T, 1978-89, 1991-; Conrail 1978-87, 1991-97; Federal Trade Commission, 1979-82, 1994-96; Pennsylvania Bell, 1980; Simpson Thatcher Bartlett, 1980, 1993-98; American Association of Railroads, 1981, 1985; Math-tech, 1981; Union Pacific Railroad, 1981, 1995-99; Family Lines Rail System, 1982; Pepper, Hamilton, and Scheetz, 1981-87, 1991-98; Siemens Corp., 1982; Board of Governors of U. S. Postal Service, 1981; OECD, 1983-85, 1991-95; Sidley & Austin, 1983-89, 1991-; U.S. Postal Service, 1983-84; Echlin Inc., 1982-83; United Airlines, 1983, 1991-98; Consultants in Industry Economics, 1983-89, 1991-; Wiley, Malehorn & Sirota, 1983-89; City of Newark, 1984; Arnold & Porter, 1986-89, 1991-; Howrey & Simon, 1985-88, 1993-; Kodak, 1987-89; Crowell & Moring, 1988; Viacom 1989, 1991-98; Bell Atlantic, 1991-94; Intel, 1991-93; AOPL, 1993; IBM, 1993-96; Merck, 1993-1995; Harkins Cunningham, 1993-96; Boeing, 1993-98; Niagra Mohawk, 1994; PSE&G, 1994-1996; Microsoft, 1994; Coca-Cola Co., 1994-; Digital Equipment Corp. 1997-98; World Bank 1994-98; Inter-American Development Bank, 1997-; Steptoe & Johnson, 1997-; Air Transport Association of America, 1998; American Electric Power, 1999-; Cravath, Swaine & Moore, 1998-; Skadden Arps, 1999-; Amgen, 2000-; Comcast, 2000-; Williams & Connolly, 2000-.

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Invited Conference Presentations:

HIID International Workshop on Infrastructure Policy
"Infrastructure Privatization and Regulation" 2000

Villa Mondragone International Economic Seminar
"Competition Policy for Network and Internet Markets" 2000

New Developments in Railroad Economics: Infrastructure Investment and Access Policies
"Railroad Access, Regulation, and Market Structure" 2000

The Multilateral Trading System at the Millennium
"Efficiency Gains From Further Liberalization" 2000

Singapore " World Bank Symposium on Competition Law and Policy
"Policy Towards Cartels and Collusion" 2000

CEPS: Is It a New World?: Economic Surprises of the Last Decade
"The Internet and E-Commerce" 2000

Cutting Edge Antitrust: Issues and Enforcement Policies
"The Direction of Antitrust Entering the New Millennium" 2000

The Conference Board: Antitrust Issues in Today"s Economy
"Antitrust Analysis of Industries With Network Effects" 1999

CEPS: New Directions in Antitrust
"Antitrust in a High-Tech World" 1999

World Bank Meeting on Competition and Regulatory Policies for Development
"Economic Principles to Guide Post-Privatization Governance" 1999

1999 Antitrust Conference
"Antitrust and the Pace of Technological Development" 1999
"Restructuring the Electric Utility Industry" 1999

HIID International Workshop on Privatization, Regulatory Reform and Corporate Governance
"Privatization and Post-Privatization Regulation of Natural Monopolies" 1999

The Federalist Society: Telecommunications Deregulation: Promises Made, Potential Lost?
"Grading the Regulators" 1999

Inter-American Development Bank: Second Generation Issues In the Reform Of Public Services
"Post-Privatization Governance" 1999
"Issues Surrounding Access Arrangements" 1999

Economic Development Institute of the World Bank -- Program on Competition Policy
"Policy Towards Horizontal Mergers" 1998

Twenty-fifth Anniversary Seminar for the Economic Analysis Group of the Department of Justice
"Market Definition in Antitrust Analysis" 1998

HIID International Workshop on Privatization, Regulatory Reform and Corporate Governance
"Infrastructure Architecture and Regulation: Railroads" 1998

EU Committee Competition Conference " Market Power
"US/EC Perspective on Market Definition" 1998

Federal Trade Commission Roundtable
"Antitrust Policy for Joint Ventures" 1998

1998 Antitrust Conference
"Communications Mergers" 1998

The Progress and Freedom Foundation Conference on Competition, Convergence, and the Microsoft Monopoly
Access and Bundling in High-Technology Markets 1998

FTC Program on The Effective Integration of Economic Analysis into Antitrust Litigation
The Role of Economic Evidence and Testimony 1997

FTC Hearings on Classical Market Power in Joint Ventures
Microeconomic Analysis and Guideline 1997

World Bank Economists --Week IV Keynote
Making Markets More Effective With Competition Policy 1997

Brookings Trade Policy Forum
Competition Policy and Antidumping: The Economic Effects 1997

University of Malaya and Harvard University Conference on The Impact of Globalisation and Privatisation on Malaysia and Asia in the Year 2020
Microeconomics, Privatization, and Vertical Integration 1997

ABA Section of Antitrust Law Conference on The Telecommunications Industry
Current Economic Issues in Telecommunications 1997

Antitrust 1998: The Annual Briefing
The Re-Emergence of Distribution Issues 1997

Inter-American Development Bank Conference on Private Investment, Infrastructure Reform and Governance in Latin America & the Caribbean
Economic Principles to Guide Post-Privatization Governance 1997

Harvard Forum on Regulatory Reform and Privatization of Telecommunications in the Middle East
Privatization: Methods and Pricing Issues 1997

American Enterprise Institute for Public Policy Research Conference
Discussion of Local Competition and Legal Culture 1997

Harvard Program on Global Reform and Privatization of Public Enterprises
"Infrastructure Privatization and Regulation: Freight" 1997

World Bank Competition Policy Workshop
"Competition Policy for Entrepreneurship and Growth" 1997

Eastern Economics Association Paul Samuelson Lecture
"Bottleneck Access in Regulation and Competition Policy" 1997

ABA Annual Meeting, Section of Antitrust Law
"Antitrust in the 21st Century: The Efficiencies Guidelines" 1997

Peruvian Ministry of Energy and Mines Conference on Regulation of Public Utilities
"Regulation: Theoretical Context and Advantages vs. Disadvantages" 1997

The FCC: New Priorities and Future Directions
"Competition in the Telecommunications Industry" 1997

American Enterprise Institute Studies in Telecommunications Deregulation
"The Scope of Competition in Telecommunications" 1996

George Mason Law Review Symposium on Antitrust in the Information Revolution
"Introduction to the Economic Theory of Antitrust and Information" 1996

Korean Telecommunications Public Lecture
"Market Opening and Fair Competition" 1996

Korea Telecommunications Forum
"Desirable Interconnection Policy in a Competitive Market" 1996

European Association for Research in Industrial Economics Annual Conference
"Bottleneck Access: Regulation and Competition Policy" 1996

Harvard Program on Global Reform and Privatization of Public Enterprises
"Railroad and Other Infrastructure Privatization" 1996

FCC Forum on Antitrust and Economic Issues Involved with InterLATA Entry
"The Scope of Telecommunications Competition" 1996

Citizens for a Sound Economy Policy Watch on Telecommunications Interconnection
"The Economics of Interconnection" 1996

World Bank Seminar on Experiences with Corporatization
"Strategic Directions of Privatization" 1996

FCC Economic Forum on the Economics of Interconnection
Lessons from Other Industries 1996

ABA Annual Meeting, Section of Antitrust Law
The Integration, Disintegration, and Reintegration
of the Entertainment Industry 1996

Conference Board: 1996 Antitrust Conference
How Economics Influences Antitrust and Vice Versa 1996

Antitrust 1996: A Special Briefing
Joint Ventures and Strategic Alliances 1996

New York State Bar Association Section of Antitrust Law Winter Meeting
Commentary on Horizontal Effects Issues 1996

FTC Hearings on the Changing Nature of Competition in a Global and
Innovation-Driven Age
Vertical Issues for Networks and Standards 1995

Wharton Seminar on Applied Microeconomics
Access Policies with Imperfect Regulation 1995

Antitrust 1996, Washington D.C.
Assessing Joint Ventures for Diminution of Competition 1995

ABA Annual Meeting, Section of Antitrust Law
Refusals to Deal -- Economic Tests for Competitive Harm 1995

FTC Seminar on Antitrust Enforcement Analysis
Diagnosing Collusion Possibilities 1995

Philadelphia Bar Education Center: Antitrust Fundamentals
Antitrust--The Underlying Economics 1995

Vanderbilt University Conference on Financial Markets
Why Do Christie and Schultz Infer Collusion From Their Data? 1995

ABA Section of Antitrust Law Chair's Showcase Program
Discussion of Telecommunications Competition Policy 1995

Conference Board: 1995 Antitrust Conference
Analysis of Mergers and Joint Ventures 1995

ABA Conference on The New Antitrust: Policy of the '90s
Antitrust on the Super Highways/Super Airways 1994

ITC Hearings on The Economic Effects of Outstanding Title VII Orders
"The Economic Impacts of Antidumping Policies" 1994

OECD Working Conference on Trade and Competition Policy
"Empirical Evidence on The Nature of Anti-dumping Actions" 1994

Antitrust 1995, Washington D.C.
"Rigorous Antitrust Standards for Distribution Arrangements" 1994

ABA -- Georgetown Law Center: Post Chicago-Economics: New Theories - New Cases?
"Economic Foundations for Vertical Merger Guidelines" 1994

Conference Board: Antitrust Issues in Today's Economy
"New Democrats, Old Agencies: Competition Law and Policy" 1994

Federal Reserve Board Distinguished Economist Series
"Regulated Private Enterprise Versus Public Enterprise" 1994

Institut d'Etudes Politiques de Paris
"Lectures on Competition Policy and Privatization" 1993

Canadian Bureau of Competition Policy Academic Seminar Series, Toronto.
"Public Versus Regulated Private Enterprise" 1993

CEPS Symposium on The Clinton Administration: A Preliminary Report Card
"Policy Towards Business" 1993

Columbia Institute for Tele-Information Conference on Competition in Network Industries, New York, NY
"Discussion of Deregulation of Networks: What Has Worked and What Hasn't" 1993

World Bank Annual Conference on Development Economics
"Public Versus Regulated Private Enterprise" 1993

Center for Public Utilities Conference on Current Issues Challenging the Regulatory Process, Santa Fe, NM
"The Economics of Current Issues in Telecommunications Regulation" 1992
"The Role of Markets in Presently Regulated Industries" 1992

The Conference Board's Conference on Antitrust Issues in Today's Economy, New York, NY
"Antitrust in the Global Economy" 1992
"Monopoly Issues for the '90s" 1993

Columbia University Seminar on Applied Economic Theory, New York, NY
"Economic Rationales for the Scope of Privatization" 1992

Howrey & Simon Conference on Antitrust Developments, Washington, DC
"Competitive Effects of Concern in the Merger Guidelines" 1992

Arnold & Porter Colloquium on Merger Enforcement, Washington, DC
"The Economic Foundations of the Merger Guidelines" 1992

American Bar Association, Section on Antitrust Law Leadership Council Conference, Monterey, CA
"Applying the 1992 Merger Guidelines" 1992

OECD Competition Policy Meeting, Paris, France
"The Economic Impacts of Antidumping Policy" 1992

Center for Public Choice Lecture Series, George Mason University Arlington, VA
"The Economic Impacts of Antidumping Policy" 1992

Brookings Institution Microeconomics Panel, Washington, DC,
"Discussion of the Evolution of Industry Structure" 1992

AT&T Conference on Antitrust Essentials
"Antitrust Standards for Mergers and Joint Ventures" 1991

ABA Institute on The Cutting Edge of Antitrust: Market Power
"Assessing and Proving Market Power: Barriers to Entry" 1991

Second Annual Workshop of the Competition Law and Policy Institute of New Zealand
"Merger Analysis, Industrial Organization Theory, and Merger Guidelines" 1991
"Exclusive Dealing and the Fisher & Paykel Case" 1991

Special Seminar of the New Zealand Treasury
"Strategic Behavior, Antitrust, and The Regulation of Natural Monopoly" 1991

Public Seminar of the Australian Trade Practices Commission
"Antitrust Issues of the 1990's" 1991

National Association of Attorneys General Antitrust Seminar
"Antitrust Economics" 1991

District of Columbia Bar's 1991 Annual Convention
"Administrative and Judicial Trends in Federal Antitrust Enforcement" 1991

ABA Spring Meeting
"Antitrust Lessons From the Airline Industry" 1991

Conference on The Transition to a Market Economy - Institutional Aspects
"Anti-Monopoly Policies and Institutions" 1991

Conference Board's Thirtieth Antitrust Conference
"Antitrust Issues in Today's Economy" 1991

American Association for the Advancement of Science Annual Meeting
"Methodologies for Economic Analysis of Mergers" 1991

General Seminar, Johns Hopkins University
"Economic Rationales for the Scope of Privatization" 1991

Capitol Economics Speakers Series
"Economics of Merger Guidelines" 1991

CRA Conference on Antitrust Issues in Regulated Industries
"Enforcement Priorities and Economic Principles" 1990

Pepper Hamilton & Scheetz Anniversary Colloquium
"New Developments in Antitrust Economics" 1990

PLI Program on Federal Antitrust Enforcement in the 90's
"The Antitrust Agenda of the 90's" 1990

FTC Distinguished Speakers Seminar
"The Evolving Merger Guidelines" 1990

The World Bank Speakers Series
"The Role of Antitrust Policy in an Open Economy" 1990

Seminar of the Secretary of Commerce and Industrial Development of Mexico
"Transitions to a Market Economy" 1990

Southern Economics Association
"Entry in Antitrust Analysis of Mergers" 1990
"Discussion of Strategic Investment and Timing of Entry" 1990

American Enterprise Institute Conference on Policy Approaches to the Deregulation of Network Industries
"Discussion of Network Problems and Solutions" 1990

American Enterprise Institute Conference on Innovation, Intellectual Property, and World Competition
"Law and Economics Framework for Analysis" 1990

Banco Nacional de Desenvolvimento Economico Social Lecture
"Competition Policy: Harnessing Private Interests for the Public Interest" 1990

Western Economics Association Annual Meetings	
"New Directions in Antitrust from a New Administration"	1990
"New Directions in Merger Enforcement: The View from Washington"	1990
Woodrow Wilson School Alumni Colloquium	
"Microeconomic Policy Analysis and Antitrust--Washington 1990"	1990
Arnold & Porter Lecture Series	
"Advocating Competition"	1991
"Antitrust Enforcement"	1990
ABA Antitrust Section Convention	
"Recent Developments in Market Definition and Merger Analysis"	1990
Federal Bar Association	
"Joint Production Legislation: Competitive Necessity or Cartel Shield?"	1990
Pew Charitable Trusts Conference	
"Economics and National Security"	1990
ABA Antitrust Section Midwinter Council Meeting	
"Fine-tuning the Merger Guidelines"	1990
"The State of the Antitrust Division"	1991
International Telecommunications Society Conference	
"Discussion of the Impact of Telecommunications in the UK"	1989
The Economists of New Jersey Conference	
"Recent Perspectives on Regulation"	1989
Conference on Current Issues Challenging the Regulatory Process	
"Innovative Pricing and Regulatory Reform"	1989
"Competitive Wheeling"	1989
Conference Board: Antitrust Issues in Today's Economy	
"Foreign Trade Issues and Antitrust"	1989
McKinsey & Co. Mini-MBA Conference	
"Economic Analysis of Pricing, Costing, and Strategic Business Behavior"	1989 1994

Olin Conference on Regulatory Mechanism Design
"Revolutions in Regulatory Theory and Practice: Exploring The Gap" 1989

University of Dundee Conference on Industrial Organization and Strategic Behavior
"Mergers in Differentiated Product Industries" 1988

Leif Johanson Lectures at the University of Oslo
"Normative Issues in Industrial Organization" 1988

Mergers and Competitiveness: Spain Facing the EEC
"Merger Policy" 1988
"R&D Joint Ventures" 1988

New Dimensions in Pricing Electricity
"Competitive Pricing and Regulatory Reform" 1988

Program for Integrating Economics and National Security: Second Annual Colloquium
"Arming Decisions Under Asymmetric Information" 1988

European Association for Research in Industrial Economics
"U.S. Railroad Deregulation and the Public Interest" 1987
"Economic Rationales for the Scope of Privatization" 1989
"Discussion of Licensing of Innovations" 1990

Annenberg Conference on Rate of Return Regulation in the Presence of Rapid Technical Change
"Discussion of Regulatory Mechanism Design in the Presence of Research, Innovation, and Spillover Effects" 1987

Special Brookings Papers Meeting
"Discussion of Empirical Approaches to Strategic Behavior" 1987
"New Merger Guidelines" 1990

Deregulation or Regulation for Telecommunications in the 1990's
"How Effective are State and Federal Regulations?" 1987

Conference Board Roundtable on Antitrust
"Research and Production Joint Ventures" 1990
"Intellectual Property and Antitrust" 1987

Current Issues in Telephone Regulation
"Economic Approaches to Market Dominance: Applicability of Contestable Markets" 1987

Harvard Business School Forum on Telecommunications
"Regulation of Information Services" 1987

The Fowler Challenge: Deregulation and Competition in The Local Telecommunications Market
"Why Reinvent the Wheel?" 1986

World Bank Seminar on Frontiers of Economics
"What Every Economist Should Know About Contestable Markets" 1986

Bell Communications Research Conference on Regulation and Information
"Fuzzy Regulatory Rules" 1986

Karl Eller Center Forum on Telecommunications
"The Changing Economic Environment in Telecommunications: Technological Change and Deregulation" 1986

Railroad Accounting Principles Board Colloquium
"Contestable Market Theory and ICC Regulation 1986

Canadian Embassy Conference on Current Issues in Canadian -- U.S. Trade and Investment
"Regulatory Revolution in the Infrastructure Industries" 1985

Eagleton Institute Conference on Telecommunications in Transition
"Industry in Transition: Economic and Public Policy Overview" 1985

Brown University Citicorp Lecture
"Logic of Regulation and Deregulation" 1985

Columbia University Communications Research Forum
"Long Distance Competition Policy" 1985

American Enterprise Institute Public Policy Week
"The Political Economy of Regulatory Reform" 1984

MIT Communications Forum
"Deregulation of AT&T Communications" 1984

Bureau of Census Longitudinal Establishment Data File and Diversification Study Conference
"Potential Uses of The File" 1984

Federal Bar Association Symposium on Joint Ventures
"The Economics of Joint Venture Assessment" 1984

Hoover Institute Conference on Antitrust
"Antitrust for High-Technology Industries" 1984

NSF Workshop on Predation and Industrial Targeting
"Current Economic Analysis of Predatory Practices" 1983

The Institute for Study of Regulation Symposium: Pricing Electric, Gas, and Telecommunications Services Today and for the Future
"Contestability As A Guide for Regulation and Deregulation" 1984

University of Pennsylvania Economics Day Symposium
"Contestability and Competition: Guides for Regulation and Deregulation" 1984

Pinhas Sapir Conference on Economic Policy in Theory and Practice
"Corporate Governance and Market Structure" 1984

Centre of Planning and Economic Research of Greece
"Issues About Industrial Deregulation" 1984
"Contestability: New Research Agenda" 1984

Hebrew and Tel Aviv Universities Conference on Public Economics
"Social Welfare Dominance Extended and Applied to Excise Taxation" 1983

NBER Conference on Industrial Organization and International Trade
"Perspectives on Horizontal Mergers in World Markets" 1983

Workshop on Local Access: Strategies for Public Policy
"Market Structure and Government Intervention in Access Markets" 1982

NBER Conference on Strategic Behavior and International Trade
"Industrial Strategy with Committed Firms: Discussion" 1982

Columbia University Graduate School of Business, Conference on Regulation and New Telecommunication Networks
"Local Pricing in a Competitive Environment" 1982

International Economic Association Roundtable Conference on New Developments in the Theory of Market Structure
"Theory of Contestability" 1982
"Product Dev., Investment, and the Evolution of Market Structures" 1982

N.Y.U. Conference on Competition and World Markets: Law and Economics
"Competition and Trade Policy--International Predation" 1982

CNRS-ISPE-NBER Conference on the Taxation of Capital
"Welfare Effects of Investment Under Imperfect Competition" 1982

Internationales Institut fur Management und Verwalturg Regulation Conference
"Welfare, Regulatory Boundaries, and the Sustainability of Oligopolies" 1981

NBER-Kellogg Graduate School of Management Conference on the Econometrics of Market Models with Imperfect Competition
"Discussion of Measurement of Monopoly Behavior: An Application to the Cigarette Industry" 1981

The Peterkin Lecture at Rice University
"Deregulation: Ideology or Logic?" 1981

FTC Seminar on Antitrust Analysis
"Viewpoints on Horizontal Mergers 1982
"Predation as a Tactical Inducement for Exit" 1980

NBER Conference on Industrial Organization and Public Policy
"An Economic Definition of Predation" 1980

The Center for Advanced Studies in Managerial Economics Conference on The Economics of Telecommunication
"Pricing Local Service as an Input" 1980

Aspen Institute Conference on the Future of the Postal Service
"Welfare Economics of Postal Pricing" 1979

Department of Justice Antitrust Seminar
"The Industry Performance Gradient Index" 1979

Eastern Economic Association Convention
"The Social Performance of Deregulated Markets for Telecom Services" 1979

Industry Workshop Association Convention
"Customer Equity and Local Measured Service" 1979

Symposium on Ratemaking Problems of Regulated Industries
"Pricing Decisions and the Regulatory Process" 1979

Woodrow Wilson School Alumni Conference
"The Push for Deregulation" 1979

NBER Conference on Industrial Organization
"Intertemporal Sustainability" 1979

World Congress of the Econometric Society
"Theoretical Industrial Organization" 1980

Institute of Public Utilities Conference on Current Issues in Public Utilities Regulation
"Network Access Pricing" 1978

ALI-ABA Conference on the Economics of Antitrust
"Predatoriness and Discriminatory Pricing" 1978

AEI Conference on Postal Service Issues
"What Can Markets Control?" 1978

University of Virginia Conference on the Economics of Regulation
"Public Interest Pricing" 1978

DRI Utility Conference
"Marginal Cost Pricing in the Utility Industry: Impact and Analysis" 1978

International Meeting of the Institute of Management Sciences
"The Envelope Theorem" 1977

University of Warwick Workshop on Oligopoly
"Industry Performance Gradient Indexes" 1977

North American Econometric Society Convention	
"Intertemporal Sustainability"	1979
"Social Welfare Dominance"	1978
"Economies of Scope, DAIC, and Markets with Joint Production"	1977
Telecommunications Policy Research Conference	
"Transition to Competitive Markets"	1986
"InterLATA Capacity Growth, Capped NTS Charges and Long Distance Competition"	1985
"Market Power in The Telecommunications Industry"	1984
"FCC Policy on Local Access Pricing"	1983
"Do We Need a Regulatory Safety Net in Telecommunications?"	1982
"Anticompetitive Vertical Conduct"	1981
"Electronic Mail and Postal Pricing"	1980
"Monopoly, Competition and Efficiency": Chairman	1979
"A Common Carrier Research Agenda"	1978
"Empirical Views of Ramsey Optimal Telephone Pricing"	1977
"Recent Research on Regulated Market Structure"	1976
"Some General Equilibrium Views of Optimal Pricing"	1975
National Bureau of Economic Research Conference on Theoretical Industrial Organization	
"Compensating Variation as a Measure of Welfare Change"	1976
Conference on Pricing in Regulated Industries: Theory & Application	
"Ramsey Optimal Pricing of Long Distance Telephone Services"	1977
NBER Conference on Public Regulation	
"Income Distributional Concerns in Regulatory Policy-Making"	1977
Allied Social Science Associations National Convention	
"Merger Guidelines and Economic Theory"	1990
Discussion of "Competitive Rules for Joint Ventures"	1989
"New Schools in Industrial Organization"	1988
"Industry Economic Analysis in the Legal Arena"	1987
"Transportation Deregulation"	1984
Discussion of "Pricing and Costing of Telecommunications Services"	1983
Discussion of "An Exact Welfare Measure"	1982
"Optimal Deregulation of Telephone Services"	1982
"Sector Differentiated Capital Taxes"	1981
"Economies of Scope"	1980
"Social Welfare Dominance"	1980

"The Economic Definition of Predation"	1979
Discussion of "Lifeline Rates, Succor or Snare?"	1979
"Multiproduct Technology and Market Structure"	1978
"The Economic Gradient Method"	1978
"Methods for Public Interest Pricing"	1977
Discussion of "The Welfare Implications of New Financial Instruments"	1976
"Welfare Theory of Concentration Indices"	1976
Discussion of "Developments in Monopolistic Competition Theory"	1976
"Hedonic Price Adjustments"	1975
"Public Good Attributes of Information and its Optimal Pricing"	1975
"Risk Invariance and Ordinally Additive Utility Functions"	1974
"Consumer's Surplus: A Rigorous Cookbook"	1974

University of Chicago Symposium on the Economics of Regulated Public Utilities
"Optimal Prices for Public Purposes" 1976

American Society for Information Science
"The Social Value of Information: An Economist's View" 1975

Institute for Mathematical Studies in the Social Sciences Summer Seminar
"The Sustainability of Natural Monopoly" 1975

U.S.-U.S.S.R. Symposium on Estimating Costs and Benefits of Information Services
"The Evaluation of the Economic Benefits of Productive Information" 1975

NYU-Columbia Symposium on Regulated Industries
"Ramsey Optimal Public Utility Pricing" 1975

Research Seminars:

Bell Communications Research (2)	University of California, San Diego
Bell Laboratories (numerous)	University of Chicago
Department of Justice (3)	University of Delaware
Electric Power Research Institute	University of Florida
Federal Reserve Board	University of Illinois
Federal Trade Commission (4)	University of Iowa (2)
Mathematica	Universite Laval

Rand
World Bank (3)
Carleton University
Carnegie-Mellon University
Columbia University (4)
Cornell University (2)
Georgetown University
Harvard University (2)
Hebrew University
Johns Hopkins University (2)
M. I. T. (4)
New York University (4)
Northwestern University (2)
Norwegian School of Economics and Business Administration
University of Maryland
University of Michigan
University of Minnesota
University of Oslo
University of Pennsylvania (3)
University of Toronto
University of Virginia
University of Wisconsin
University of Wyoming
Vanderbilt University
Yale University (2)
Princeton University (many)
Rice University
Stanford University (5)
S.U.N.Y. Albany

Before the

Surface Transportation Board

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Public Views on Major Rail Consolidations

Verified Statement of

Robert D. Willig

I, Robert D. Willig, verify under penalty of perjury that the following is true and correct. Further, I certify that I am qualified and authorized to file this Verified Statement.

Executed the 9th day of January, 2001.

Robert D. Willig

Robert D. Willig